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IN THE MATTER OF "THE NATURAL GAS UTILITIES ACT"

—and—

IN THE MATTER OF an Enquiry into Scheme to be adopted for Gathering, Processing and Transmission of Natural Gas in Turner Valley

G. M. BLACKSTOCK, Esq., K.C., *Chairman*

Dr. E. H. BOOMER, F.C.I.C., *Commissioner*

Session:

CALGARY, Alberta June 20th, 1946

VOLUME 90

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I N D E X

VOLUME 90

June 20th, 1946.

	Page
ARGUMENT BY MR. FENERTY (Continued).....	7338
ARGUMENT BY MR. BLANCHARD.....	7340
ARGUMENT BY MR. HAMILTON.....	7368
ARGUMENT BY MR. BLANCHARD (Continued).....	7379
ARGUMENT BY MR. CHAMBERS.....	7389

E X H I B I T S

No.		
194	Financial submission by Mr. Hamilton.....	7365

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MR. FENERTY: Mr. Chairman, with your permission I want to say one more word on a point, and I told my learned friends I would not be more than two minutes. I do not think they believed me, but I am not going to.

This matter is of some importance, and it refers to my argument made on Section 49(2), and I am afraid that I may have left the impression with the Board and with Counsel that I was founding my entire argument on the use of the word "taken". I did base it on the answer by Mr. Hamilton that he give me one stronger case for the application of the book depreciation, that is, where the former owner was a public utility, but I want to point out now that that argument is much broader than that and it in no sense depends upon the word "taken". I do not care what word has been used there.

I pointed out that if it had not intended to include owners other than public utilities, the Act would have said so, and my friend, Mr. Harvie, referred me to a definition of the word "Owner" in the Act. And the definition in the Act says that the word "Owner" means, "Unless the context otherwise requires, means and includes in addition to its ordinary meaning, the person who is operating any oil well or capable of producing natural gas or who is in charge of the management of such well."

Now that makes it quite clear, that not only do they not exclude previous public utility owners, but they are included.

Now if Mr. Hamilton is correct that there is one case stronger for the application of that sentence,

that is where the former owner is a public utility, it follows that in the case of the owner under the definition of the Act, that is not a public utility, that that is the strongest case for that application.

I say if we take the strongest case for the application to an owner that is not a public utility, or the depreciation taken by a former owner who was not a public utility, and we do not apply it we have discarded the Act and rendered it meaningless, whether or not the owner was a public utility. We have discarded it completely and there is no meaning to the Act unless we apply it in the strongest case.

And as I said before, the consequences are very wide, that if this is not a case where it must be applied, and if the Act is to be given any meaning, it follows from that then that we are back to book values. I said I would only be two minutes and I am through.

THE CHAIRMAN: Mr. Blanchard?

.....

ARGUMENT BY MR. BLANCHARD

MR.BLANCHARD: Mr. Chairman, at this stage, after all other Counsel have addressed you, it is a little difficult for me to know just where to start, and possibly it will be even more difficult for me to know where to stop. Fortunately, Counsel who have preceded me in their very able and exhaustive addresses, have covered every phase of this Inquiry from every standpoint, and I do not know that there is much that I can say, perhaps nothing that I can say, that will be of any great assistance to the Board, except to express my views as agent of the Attorney General, as to some of the matters that I consider of first rate importance, and whether you accept the whole or any part of my views, of course, is beside the point, Sir.

Now, I think I do not need to deal with some of the very important matters that have been cleared away pretty well as we have gone along. I accept the estimates finally made by Dr. Katz, Mr.Stevens Guille and Mr. Connell with respect to the recoverable dry reserves. I think those are very conveniently set out in Mr. Chambers' argument at pages 6573 to 6577, by way of crystallizing the results.

Then I think there is no contention with regard to market sharing matters. There might be some slight difference, but I have not detected them between Mr. Chambers' submission and Mr. Harvie's and Mr. McDonald's, in that respect. But there is no matter of contention there that I need to deal with. The same is true, Sir, and I accept the final estimates of Mr. Brownie with respect to the market demand estimate in the next two or three years. Incidentally, those estimates make a slight difference in the

ARGUMENT BY MR. HAWKINS.

MR. HAWKINS: Mr. Chairman, at this stage, after all other Counsel have addressed you, it is a little difficult for me to know just where to start, and possibly it will be even more difficult for me to know where to stop. Fortunately, Counsel had have preceded me in their very able and exhaustive addresses, have covered every phase of this inquiry from every standpoint, and I do not know that there is much that I can say, perhaps nothing that I can say, that will be of any great assistance to the Board, except to express my views as agent of the Attorney General, on some of the matters that I consider of first rate importance, and whether you accept the whole or any part of my views, of course, is beside the point, Sir.

Now, I think I do not need to deal with some of the very important matters that have been cleared away pretty well as we have gone along. I accept the estimates made by Dr. Rae, Mr. Stevens, Guile and Mr. Connell with regard to the recoverable dry reserves. I think those are very conveniently set out in Mr. Chambers' argument at pages 6013 to 6017, by way of establishing the results.

Then I think there is no controversy with regard to market sharing matters. There might be some slight differences, but I have not detected them between Mr. Chambers' submission and Mr. Harvie's and Mr. McDonald's, in that respect. But there is no matter of controversy there that I need to deal with. The same is true, Sir, and I accept the final estimates of Mr. Bowzie with respect to the market demand estimate in the next two or three years. Finally, these estimates make a slight difference in the

submissions that have been made by Mr. Hamilton, and, of course, his figures will have to be adjusted accordingly.

So that, Sir, I will first come to and deal with, not at any length, the Madison rate base. Now, I had intended to discuss the principles of rate determination as they seemed to me, but in view of Mr. Steer's very able and excellent discussion on that subject, I am glad to be relieved of saying anything further with respect to it. I certainly could not have dealt with it nearly as satisfactorily as Mr. Steer, and the same applies to his remarks with reference to depreciation where historical cost is taken as the basis.

Incidentally, with respect to the question of adopting throughput accrued depreciation, I think I might remind the Board that when I was discussing gathering lines with Mr. Hill, and we found that on his computations he had given a life of approximately 105 years to the gathering lines, and not 50 years, and when it was called to his attention that the life of the field might not be more than another 25 to 30years, and that the salvage of those lines would at no time be greater than 5%, Mr. Hill agreed that depletion should be taken into account, in calculating accrued depreciation. Now, when he said that, he admitted a principle that has been applied by Mr. Hamilton in his submission. In other words, where the structures and installations in natural gas fields will outlive the field, then it is proper to apply the depletion factor, that is, throughput depreciation.

And to that same effect is the evidence of Professor Stewart in Exhibit 131, and I do not think I need to take the time of the Board in discussing it.

Now, Mr. McDonald, in his address,

appears to have taken the view that Professor Stewart concurred with what Mr. Chambers had said as to the adoption of reproduction cost new in arriving at a rate base for the utility. And I think if you, Mr. Chairman, will refer to Volume 55, pages 4322 to 4324, which is part of Professor Stewart's evidence, you will find that Professor Stewart by no means adopted the views of Mr. Chambers as to the application of reproduction cost new.

And it strikes me, although I think Mr.Steer has dealt with it quite fully, that Professor Stewart's discussion of the subject of fair value is evidence that should be of some value to this Board. I am going to mention it because the question of fairness is of the greatest importance. No one, at least I, having no axe to grind, do not want to see any party in these proceedings treated unfairly naturally, and it is important to consider what the concept of fair value involves, and Professor Stewart referred to the matter of reasonable expectation. That is discussed in Exhibit 131 and in his evidence.

Now, my impression of that evidence was this, that if an investor invests in a company having limited opportunities to make capital gain and at some later stage that company is brought under regulation, he has had a reasonable expectation that that capital gain will be recognized and that it will be taken into account when a regulatory Board comes to fix the amount ot capital upon which a rate of return will be allowed.

Now, what is the position with Royalite? That has already been canvassed by all Counsel, but I am going to speak of it again.

Here was a company whose gas division was committed to a single undertaking, and that single undertaking has a limited life, the life of the reserve. So far as its gas division was concerned, it was important to it, I assume, that those reserves should be guarded and saved, I have not got the right word, as well as possible. From other considerations, however, that was not done, and gas, as we all know, was wasted in tremendous quantities.

Now, as I say, if the gas division had only a limited life, an undertaking with a limited life, and not only that, but an undertaking whose earnings were restricted to a contractual price for all time. In later years, 7¾ cents, and not only that, but I am just going to say this, we do not know because it has not been revealed by either Madison or Royalite, what rate of return that 7¾ cents gave the company, based, let us say, on reproduction cost new, of its assets used in the gas division before this company came under regulation. We do not know that because it has not been revealed. We do know that in 1939, and I base this remark on a statement made by Mr. Chambers, or, rather, the question put by Mr. Chambers to one of the witnesses, that an effort was made by Royalite to have that seven and three-quarter cent contract price for gas at the gate of the Canadian Western revised, I presume, upwards, but without success.

(Go to page 7344)

Now they were something more than that, and I am still speaking of the reasonable expectation of the people who had money invested in the gas division of that company because that is what we are talking about. They were subject to the possibility of having the Public Utility Board - and this was from 1923 when that Act was passed - of having that price revised on application made by a municipality. Later I think in 1942 that revision could have taken place by initiation by the Board. I am not certain about that last but that is my impression. I have not looked at the Act lately.

THE CHAIRMAN: That is right.

MR. BLANCHARD: So what was the position. How could an investor in a Company, an unregulated company, the life of whose undertaking was limited by the amount of raw material that was available; whose earnings were restricted by a contract price and who would be under liability at any time to have that price revised by a regulatory Board. In other words if they were not under regulation, the price of gas was subject and liable to regulation. How could an investor in a company of that kind expect to get any more, expect any more return than a fair return on his investment and a return of his capital by proper methods of depreciation through the probable life of the field. I submit that Royalite did exactly that. The depreciation they have taken in their books may not be exactly what would have been taken on the basis I have suggested, but it would be an intelligent and proper thing for Royalite to say: "The life of our gas division is limited and we must recover our capital while we are operating it, and we should

"recover it as rapidly as possible by reason of the possibility that this price will be regulated and may be reduced and so reduce our return to a lower basis."

Now I do not know whether the 7¾ cents reflected, let us say, the reproduction new basis or the historical cost basis. I do not know whether it gave them a rate of return of 5, 10 or 15 per cent or nothing and we do not know. We can perhaps make some calculations based on the price and the amount of gas that was marketed each year. I have not done that and I do not know what the result would be.

Now what would an investor in such a concern, having all the factors in the undertaking that I have mentioned, what would he expect if his undertaking was brought wholly under regulation. Surely he had no right to expect that just by reason of regulation he was going to get a return on the whole value of the properties used in the gas division on a reconstruction or reproduction cost new basis and a rate of return given to him on that basis. So I say when we are considering this concept of fairness these are things that it is important to take into consideration and I must confess, sir, that I do not know where they lead us. I must say that I have sometimes felt that Mr. Fenerty's view, and I think perhaps Mr. Steer's, that so far as all these installations are concerned, that is up to the time of regulation, that book depreciation would be the proper depreciation under all these circumstances that we have mentioned. And I have also wondered whether if there had been a revision of that price before the Natural Gas Utilities Act was passed, under the old section of the Public

Utilities Act if there had been an Inquiry as to what would be the proper price of the gas sold by the Royalite to the Canadian Western, I have wondered whether the Public Utilities Board for one moment would have considered setting up a rate base or examining a rate base or fixing a price on the basis of reproduction cost new where this was a continuous operation and with the price liable to be regulated at any time; or whether they would have formed a basis and fixed that price on a basis of historical cost or whether they would not simply have taken the books and said: "Here you have received, you have taken so much depreciation and a fair price will be based on your books." I do not know. But the factors that would have applied to an Inquiry under the Public Utilities Act very closely apply now because the only difference is that the Company is now coming under regulation wholly as to its gas division and one added thing, they are required to share the market and to become common carriers. So my submission is that when we are applying, and if we apply historical cost and apply accrued throughput depreciation, ignoring their book depreciation on the basis of Mr. Hamilton's recommendation in Exhibit 125, my submission is that Madison has been dealt with with generosity.

Now there are some things with respect to this historical cost, suggested historical rate base, that have been attacked by Mr. Chambers because he said: "Even if you take the historical cost you have not allowed this Company certain things that should definitely have been capitalized in your reconstructed historical cost and that are used and useful and therefore the historical cost does not represent the true value at all of those assets.

The first item is - I am going to deal with them, sir, because they are such a substantial amount that it is important for the Board to give consideration to them. The first I think is an item of $69,957.00. I cannot read my own writing, sir, but I think those are the figures. In any event the odd dollars do not matter. $69,957.00, I think it is and that item appears in the Royalite books as being the intangible costs in connection with certain gathering lines and have remained on the books, but the gathering lines are not in the place where they were when that item was placed in the books. The gathering lines were relocated and the cost of relocating them was capitalized by the company and we have taken that capitalized figure into our historical cost in full. If we added the $69,000 -odd, we would be putting the cost of laying the old lines that have been taken up into the rate base. I assume that that item of 69,000 odd dollars has been left in the books for income tax purposes because it had not been fully depreciated. But why in an historical cost should we be required to pay for the laying of lines that have been taken up and relocated and then pay for laying them again in the place they are now; and since the question is: What is used and useful at the time of coming under regulation?, my submission is that there is no substance to that particular criticism made by Mr. Chambers.

Now then we come to some very substantial items and I am going to refer to them for two reasons, or to some of them I refer for two reasons. One is that Mr. Chambers says we have not given effect to them and that they are really capital items and the other reason is with respect to those contained in what was known as Project A. I want

to mention them because I think it shows the extreme desire to be fair, as Mr. Hamilton was when he compared those submissions and his recommendations. Now those items that Mr. Chambers said should go in and have not been capitalized and should have been capitalized under historical cost, they come to a total of - I have lost the place again, sir - they come to a total of $172,383.00, so that they are of importance. Those items were dealt with by Mr. Hamilton in Exhibit 146. That is he grouped those expenses under four heads and they were A, B, C and D. Now in the first place let me remind you, Sir, that Mr. Hamilton gave evidence that those items were taken into account or at least discussed by him with Mr. Kirkpatrick and I think Mr. Hamilton said other officials at the time he was preparing his historical cost figures and that at that time his impression, Mr. Hamilton's impression at any rate was that no claim was being made by Madison that those expenditures should be taken into account because there were offsetting factors that should also be taken into account.

(Go to page 7349)

I will refer to that again.

Now Group "A" of Exhibit 146 is not a great amount. It is $18,055.00 reproduction cost new without depreciation representing extension to fuel lines, valued on the Royalite books at $49.00 and that is the cost at which they were taken into Mr. Hamilton's statement.

Now if they were allowed in full on the historical cost basis we would first take off 25%, which is the percentage by which the average historical costs are below Mr. Hill's replacement cost new, and 9% for overhead and then we reduce the amount as arrived at by 27% for accrued throughput depreciation and the net result would be about sixty cents on the dollar, or $10,833.00. In other words if that item is taken at an adjustment of the historical cost by Mr. Hamilton the amount would be approximately $10,833.00.

Now those were taken into the Royalite books at $49.00, but Mr. Hamilton was shown where it was customary to expense extensions to fuel lines of that character, that was explained to him and we accepted that and Mr. Hamilton says, and he has stated in his evidence, that if those items stood alone he would not object to them but they are confined, - there are a number of other items too and they all come into these off -setting items.

Now Group "B" is a great deal more important. I will try and deal with this more briefly. I am taking a good deal of time but they are a substantial item as they are raised by Mr. Chambers.

Group "B" were items having a value under the reproduction costs new basis of $78,075.00. We have allowed them on the original cost at $73,085.85. Now if allowed on the

original or historical cost it would be about fifty thousand dollars, applying the same factors which I mentioned before.

Now in this category, the equipment is there but we have no evidence of where the original cost has been charged. The items were in existence, as in Group "A", so far as we could ascertain. Mr. Stevens-Guille could give us the history of those items but he could not say that they were charged in the books, he could not show where, - that they were charged in the books or where the instructions came from or how they came to be in their present location.

Now theoretically, Mr. Hamilton says the original cost may be in any one of three places:

(a) They may have been written off to expense account of Royalite in past years and have accordingly reduced the profits in those years, or

(b) They may have been capitalized as an element of the historical cost of the plant still in the hands of Royalite, or

(c) They may have been included in the cost of something else which is already included in the total costs of the plant taken over by Madison.

Those items must have been charged some place, with the double entry book keeping system in use by Royalite. They could not simply disappear, and Mr. Hamilton's final conclusion, having regard to the fact that the books of Royalite were kept with great care is that the money spent in acquiring or fabricating the items in that group have found themselves into some other place that has already been taken into account in the historical costs.

Now then we come to Group "C", a total of

$52,958.55.

Now those were the expenditures made by Royalite in connection with the experimentation with the Girbotol plant and that item, which Mr. Chambers now asks should be taken into account and added to historical costs, includes the contaminated chemical which still is in the possession of the Company in a Royalite tank and has never been, - the ownership of it has never passed to Madison and you are asked to take that into the historical costs rate base.

Now if you will remember the evidence of Mr. Kirkpatrick when he first gave evidence, I think I am right, yes, in Volume 32, Page 1827, Mr. Kirkpatrick said that that would not be capitalized in the Madison books and that Royalite was taking the loss of that contaminated chemical. That attitude has been changed and we are now asked to bring into the historical costs rate base $32,000.00 for the chemical that is not used and cannot be useful. Mr. Hamilton thinks that should not be done and I have adopted his view.

Now then the rest, the Royalite actually expensed this $52,958.55 and they capitalized about twenty thousand dollars of that experimental work and of course what was capitalized has been taken into our historical costs. I would suggest this, that possibly this experimentation has been for the benefit of the Madison Company and that perhaps some consideration might be given to an allowance, a reasonable allowance, for the experimentation, remembering of course that Royalite enjoyed the fruits of those successful experiments for several years before this Company came under regulation.

MR. CHAMBERS: Not several years, Mr. Blanchard.

MR. BLANCHARD: I think from 1941 on, or 1942.

MR. CHAMBERS: The end of 1942.

MR. BLANCHARD: Perhaps two years, I do not want to exaggerate it in any way. I simply say it should be taken into, the enjoyment which Royalite had, from this successful experimentation should be taken into consideration, and if the Board sees fit to make some adjustment to give effect to those experimental costs all right, but certainly we do not think that any effect should be given to the cost of this contaminated chemical.

So much for that item for $52,950.00.

Now the next group and the last group is Group "D" and that amounts to $22,294.07.

Now all the items in this group that were capitalized were allowed by Mr. Hamilton in his historical costs and they were allowed at the abnormal cost figures. They are part of projects "A" which you will remember was a project undertaken pursuant to the provision of the contract made between Imperial Oil and the Allied War Services or the Minister of National Defence, I have forgotten which, and that project involved the expenditures of very large amounts of money. The costs incurred in connection with that project were expensed by Royalite or carried in a suspense account, perhaps it would be better to say, all through 1944 and no final disposition was made, from an accounting point of view, until January 1945, a year after Madison had come under regulation. Then they made their disposition of this very large expenditure and $283,700.00 was assigned as the cost of items already in Mr. Hill's 1943 appraisal. $287,200.00 was assigned as the capital cost of items in regard to Madison, namely the

gasoline plant and the north return fuel lines and some lab. equipment I think.

Then $68,700.00 was written off by Royalite to expense, so out of this project "A" Madison took over many of the assets that were involved, that were installed under that, and they were taken into account in Mr. Hill's, no, - they were not taken in account in Mr. Hill's appraisal but they were taken into our historical costs at $283,700.00. In Mr. Hill's appraisal on reproduction costs new they were taken in at a great deal less figure and I am going to deal with that in a minute.

Now then, calculated in the costs of the assets which were not to be transferred to Madison were the consolidation of the #2 and the #1 gasoline plant and in the disposition made in 1945 of $37,800.00, which had been spent in and around the boiler plant consolidation, the Royalite capitalized $9,000.00 and that is in Mr. Hamilton's historical costs.

Now what appeals to me about these things is this, that they are now asking for an additional twenty-nine thousand odd dollars which was expensed and which they say are really capital items and we say "you Royalite and Madison made your disposition of this money or those expenditures which were held in the suspense account for a year after you came under regulation, and then you made your allocations as you considered was the value, the cost of the assets turned over to Madison, what that cost was and you placed it at such and such a figure", surely that is binding on them but if it is not binding on them I want to refer to this, that the amount expensed in that whole project was only sixty-eight or sixty-nine thousand dollars, - I have given the figure already, - which is an extremely low

expense figure for a project of that size and then again a great deal, there was a great deal of money spent in endeavouring to keep continuity of service while those consolidations and constructions were going on, and that made the project an extremely costly one.

Mr. Stevens-Guille gave some evidence as to the abnormality of these costs at Pages 5661 to 5665 in Volume 69 and there he says that the conditions of labour were so difficult and abnormal that this project cost a tremendous lot of money. And why did it cost so much money ? What was the necessity of doing this job so quickly and under such pressure, and I want to read part of Mr. Stevens-Guille's evidence in that connection. He said:

"Now I would like to turn to project "A" and give some details of the problem of carrying it out. I have already mentioned the labour difficulty. Originally the 150 men were expected to be provided by National Selective Service, but at no time were 150 men available on the job, and furthermore, the turnover of men was tremendous and the type of man was far from suitable for the work being undertaken. This continued right throughout the job in spite of the most urgent representations to National Selective Service right from Turner Valley to Calgary, Winnipeg, the regional centre, down to Ottawa.

Materials in 1943 were very difficult to obtain. Deliveries when dates could be obtained never made those dates. Local fabricating concerns such as for example, Dominion Bridge were at that time making high priority material for the ship building industry. It was under conditions such as these that we were instructed to proceed with the utmost diligence and in the contracts you

will see the words 'expeditious' and 'earliest date' mentioned."

In other words it was because the contract Exhibit 147 required this work to be done immediately that it was done at such an abnormal expense and not for the sole purposes of meeting the gas market demands.

Now I turn again to what Mr. Stevens-Guille said about this on cross-examination at Page 5695 (Volume 69)

"Q Now then as you have mentioned, the normal cost incurred under these installations in 1943 particularly resulted in a very much higher historical cost than reproduction cost ?

A That is correct.

Q All these installations and that one might say would very largely offset the lower historical cost in earlier years as compared with reproduction costs of earlier years ?

A Yes, it would have that effect, Mr. Blanchard. Of course bearing in mind that while the appraisal was made in 1943, the appraisal decided to disregard the fact that a lot of this work was done at that time and might possibly therefore fairly carry the higher cost as reproduction cost of that year.

Q I understood you to say that the historical cost was double the reproduction ? (That is the cost in the books)

A On certain items. I never made that as a general sweeping statement to cover all the installations,...."

But as a matter of fact that was made by Mr. Stevens-Guille at an earlier point in one of the pages I

have already mentioned. Yes, at Page 5665:

"All these things do build up a cost".

After giving the reasons for the necessity of doing it at once, the tremendous cost involved, he says:

"All these things do build up a cost, and in this case I think Mr. Hamilton's figures showed the historical figure on the books is more than twice the reproduction cost that Mr. Hill allowed."

And that applies to all of project "A". In other words I suggest this, sir, that Mr. Hamilton in his submission and in his recommendation is being more than generous and we are being more than fair when we allow the historical costs of these items that go into the picture under such abnormal conditions and which appear in the books at over double or in that neighbourhood of the figure that Mr. Hill himself put on those as being the value of reproduction costs new.

I suggest when effect is given and we take into account and give effect as historical costs to abnormal costs at that time I think it might very well occur to the Board that there should be some reduction if anything in the historical cost to meet that situation.

Certainly no further allowance should be made of items that were expensed by Royalite and which they now seek to have taken into capital accounts under those conditions and I say if there are any hidden costs, historical costs, in the other group that should have been taken into account that they are more than offset by the considerations that I have mentioned and I submit therefore that no effect whatever should be given to the criticisms of Mr. Chambers with respect to those very substantial items.

Incidentally I have a note here that we allowed under pure misapprehension and still in the historical costs figures $8307.00 which was part of project "A". It was for transportion and camp expenses.

THE CHAIRMAN: That would be charged to operation at that time.

MR. BLANCHARD: Yes, but we have it in another place. It is included in the 9% overhead.

THE CHAIRMAN: The time Royalite incurred that expense it was for transporting men and camp expenses. That would go through as an operating charge in their books.

MR. HAMILTON: It was part of the total cost of project "A" and was dealt with at the time of cleaning it up in 1945.

MR. BLANCHARD: But we have given effect to 9% overhead. Perhaps I should have found that out before I started to address the Board.

MR. HAMILTON: The situation is this that we attempted to in adjusting the historical costs to allow for construction tools and transportation and also general overhead and that set off allowance was deemed to cover items of this character and then we found we have allowed in specific cases and also allowed it in the overhead cost in addition.

MR. BLANCHARD: That I think is all I have to deal with on the question of the Madison rate base. As I say the principles upon which it should be adopted, that is the historical costs, that is the revised historical costs, have been dealt with fully by Mr. Steer.

The result of that is that so far as I am concerned, I do not know whether the Board will be or not, but so far as I am concerned I accept Mr. Hamilton's recommendation

contained in his Exhibit 125 that the $1,573,000,000 plus working capital which I am going to deal with and plus the Girbotol advance royalites to be taken as the amount of capital from which this company may earn a rate of return, but I think perhaps effect should be given at this time to salvage. That is a matter for the consideration of the Board.

It has been suggested that salvage be dealt with at some future time on an application as to rates or on another hearing later on but it seems to me the principle should be admitted now and the principle is of course that utilities shall not be allowed to make a capital gain when its rate base has been fully amortized.

If effect is given to salvage then the recommendation of Mr. Hamilton as contained in Exhibit 125 will be changed to accord with the figures in Exhibit 124 and in submission WH 7, but adjusting it for the changed reserves as we accept them now which would make a difference of about $1,000.00 and I think the exact figure would be having made an adjustment for the difference in the reserve $1,606,563.00.

Now I come to the British American Company. At a later time I would like to be able to glance through my notes again. The British American rate base. There we have a situation where the old installations do not amount to a great deal one way or another as compared with the investment in Madison, but when we come to consider a little later what the effect will be of taking these old lines into the rate base and of also taking into the rate base the actual expenditure made since regulation, when we come to find out the effect of that we may have to consider the rate base in relation to the

estimates that were presented to this Board in the early stages of this Hearing. This will be referred to a little later, sir.

(Go to Page 7360)

I think I had perhaps better deal with that after I have asked Mr. Hamilton to deal with that unit cost basis on certain assumptions. I will do the same with the G.O.P., sir, at that time.

As to the rate of return, I am entirely in accord with what Mr. McDonald says in that respect and I concur with him in the view that the net rate of return of 7% is fair and even a generous rate, having regard to the risk and having regard to all the other circumstances. I would put it perhaps that there is an additional reason for adopting that figure too, not mentioned by Mr. McDonald, and that is this. I think Mr. Baker in his evidence said that the average rate of return allowed to gas companies - or was it utility - I am not certain which.

MR. HAMILTON: Gas companies.

MR. BLANCHARD: Allowed to gas companies in the United States was 6½% and then he pointed out that there was a difference in the basic rate of Government securities of half of one per cent.

MR. HAMILTON: Three-quarters.

MR. BLANCHARD: Three-quarters was it, between U.S. bonds and Dominion bonds and he proceeded to say that is so many times more, that therefore the Dominion rate is so many times more than the U.S.A. rate. That is entirely fallacious. The difference is half of three-quarters of one per cent, whichever it is. That is all. It is not three times the difference. The difference is the difference exactly and that is all my suggestion is, sir, that you might give consideration or you might give weight to the fact that the average rate of return for gas companies in the United States is 6½% and add

one-half of one per cent or the difference of the basic rate of interest in the two countries and come to 7%, which would be an adjusted gross rate of 11-2/3%.

There is another matter I would like to mention. Royalite has proposed to store gas and to purchase it on a discounted basis of 8% and Mr. Baker said that was eminently a fair and proper figure. Now that is without income tax and the result of that is that Royalite is buying this gas at a discounted rate, a net discounted rate of 4.8%. That is considered by Royalite to be fair and stated by Mr. Baker to be fair. Now it seems to me that the risk Royalite is taking with respect to that re-pressured gas is fully as great as the risk that Madison is taking to recover its capital and that I think is something that is before the Board and should be taken into consideration in considering the fairness of the rate to be allowed.

Mr. Hamilton has called my attention to the fact that we are allowing, or we are taking into account and we will be carrying the full 40%, whereas the Company might have financed it some other way. Professor Stewart, you will remember, said the financial structure should be taken into account in fixing the rate of return. But that has all been discussed, sir, and I do not think I need say anything more about it. I was going to ask if we might have a 5 minute adjournment.

THE CHAIRMAN: Yes.

(At this stage there was a short adjournment taken.)

.....

THE CHAIRMAN: All right, Mr. Blanchard.

MR. BLANCHARD: Mr. Hamilton has called to my attention the fact that we cannot say that the historical cost in connection with Project A is doubled but that some items were, in fact I think you will recognize one item in which it was nearly treble the amount. It is impossible to say to what extent the historical costs are in excess of the used and useful dollars spent in that project and I perhaps exaggerated too much when I suggested that and if I did convey the suggestion that the whole thing was doubled on Hill's figures or the proper costs. I may, before leaving this question of rate base, just recall the fact that we do not give in the historical cost any effect to the obsolescence of the Seaboard and we do not capitalize the additional operating costs of operating the Seaboard, which, if reproduction costs were taken would amount to something like $76,000.00. In other words the bad is taken with the good. I just mention that because I think it is of some importance.

Now coming to working capital, sir, the suggestion of Mr. Hamilton, which I concur in, is that there should be an allowance of $140,000.00. That is set out in W.H.20 of Exhibit 124. Now Mr. Hill himself in giving evidence said that if the gas payments were staggered then he would consider $150,000.00 as ample working capital. In other words, he was prepared to knock off $40,000.00 if the gas payments were staggered. Mr. Kirkpatrick did not agree with that view, but Mr. Kirkpatrick did say that it was on Mr. Hill's recommendation that the figure of $190,000.00 was put forward by Madison. Mr. Hamilton has dealt fully with the cash requirements of the Company. We have allowed

their inventory capital in full. Now Mr. Zinder, while he admitted that in informal matters one-eighth of the early operating costs were used as a sort of rule of thumb method of getting at the working capital, that in formal hearings an examination was made of the required expenditures and working capital fixed accordingly. Professor Stewart's evidence is to the same effect. Professor Stewart said that you should not simply take some rule of thumb figure, that the necessities of the company should be considered and then the working capital fixed on an appropriate basis. Now Mr. Hamilton's figure gave something around $10,000.00 over the amount that he considers would be necessary for the wages and other requirements during the early part of the year. The contention between Madison figures and Mr. Hamilton's lies in the contingency allowance and our submission is that where a contingency arises, an unforeseen contingency, it would be perfectly proper for the company to borrow the money at the bank for a short period. It would only be for a short period and that seems an entirely reasonable thing to do. Barnes in his Economics of Public Utility Regulations, which has been referred to a number of times, on page 496 says that "it is possible and proper for a utility to meet an extraordinary requirement through borrowing." It is our submission that that view should be adopted here and that in Mr. Hamilton's figure of $140,000.00 there is ample capital, working capital, to carry on this undertaking without putting the ultimate consumer to the cost of paying interest on some $50,000.00, year in and year out, that is only required if some unforeseen contingency should arise. This amounts to $5,833.00 a year in additional interest charges if that additional $50,000.

is allowed. So that I concur with Mr. Hamilton's figure on that.

Then so far as the British American is concerned, I suggest that $15,000 and in addition such reasonable amounts as they may require to carry their inventory is a proper and a similar allowance to Gas & Oil Refineries on a proportionate basis.

THE CHAIRMAN: Have you anything to say about going value?

MR. BLANCHARD: I am just going to mention it, sir. Professor Stewaet in his evidence says that where you adopt original or historical cost, taking the good with the bad throughout, that going value should never be allowed, an intangible such as that should never be allowed unless something has actually been paid by the utility for going value. I think that is dealt with, yes, by Professor Stewart in Exhibit 131 at pages 18 and 19. And where we have, as I say, given effect to abnormal cost in connection with project A; where we are not giving any effect to the obsolescence of the Seaboard or attempting to capitalize the operating costs in connection with that installation, it seems to me that there is no sound basis on which going value should be allowed. If it is allowed it should be amortized in the same way as the rest of the rate base. I noticed in Exhibit 181 filed by my friend Mr. Chambers that his going value of $200,000.00 remains in the rate base to the end, at least to the end of the schedules that have been put in here. It strikes me that going value disappears at the same rate and should be depreciated at the same rate as anything else. You certainly have no going value at the end.

MR. CHAMBERS: We do not ask for any amortization on it in the future.

MR. BLANCHARD: No but it is carried in the rate base right along at $200,000.00.

MR. CHAMBERS: Yes.

MR. BLANCHARD: My submission is that that is wrong and in the same way it should be treated as everything else. Then we say, sir, that fuel, plant fuel should be paid for and that provision is made for that in the submission that will be filed in support of what I am saying now.

At this stage, sir, I would like to, with your permission, ask Mr. Hamilton to discuss the statement which I would like to file as an Exhibit.

SUBMISSION BY MR. HAMILTON
AS TO THE RATE BASE NOW MARKED
EXHIBIT 194.

MR. BLANCHARD: This was prepared in an endeavour to arrive at the cost of gas at the Canadian Western gate delivered from each of the three companies, the three areas, and these figures that are used, that is as to allocation of costs as between the utilities and the absorption plants are simply arbitrary in a sense. We have allocated in this statement 40% of the costs in each case to the absorption plant and 60% to the utilities as to gathering costs.

(Go to page 7366.)

Now I will discuss later the propriety of that allocation. I merely mention the fact that I do not desire to be bound at this moment by that allocation but it will afford a basis upon which this Board can see what the effect will be if such and such, - if the rate base that I have suggested should be adopted is used in the case of Madison, and with that allocation of 60/40.

In the case of the British American costs, we have taken the historical costs less throughput depreciation for old lines and we have taken their full costs with respect to the new installations the low pressure system.

MR. CHAMBERS: Pardon me, Mr. Blanchard, was Exhibit 194 prepared on the basis of the new estimates or the old?

MR. BLANCGARD: It is taken on the basis of the latest estimate we have from Mr. Brownie. There may have been a small change in that sense.

MR. CHAMBERS: I am referring to the reserves.

MR.BLANCHARD: Yes, we took that on the basis of 361 billion.

Now I think I am correct in that, that you took the new reserves and not the ones taken originally?

MR. HAMILTON: Yes.

MR. BLANCHARD: As I say, in Exhibit 194, we have taken as the rate base for the British American, the actual historical cost less accrued throughput depreciation for old lines, and we have taken their full costs of the installations since the utility came under regulation, and you will notice when dealing with Gas & Oil Refineries, we have not given any effect to gathering at all, but our suggestion is going to be that there be a token payment made to Gas & Oil Refineries, of 1 cent per thousand cubic feet of gas, and I will ask Mr.

Hamilton to deal with that, but that would be fairly close to the gathering costs, if the historical costsless throughput depreciation were taken with respect to the gathering lines in that area. We feel that, in view of the fact that there is no separation of the absorption plant and other activities of the Gas & Oil Refineries, that it is quite impossible now, and will be in the future, to keep the costs separate with respect to those lines. They have not formed a separate public utility with respect to the gathering lines and for that reason we believe that it would be fair to allow 1 cent per thousand cubic feet gathered.

Now that is going to make very little difference in the over-all picture. It would probably amount to something between 1 and 2 mills in the total cost.

Now with these explanations, Sir, I think I will ask Mr. Hamilton to discuss this statement. It is nearly self-explanatory , but there may be a number of things that he will want to deal with as to what he took into account in arriving at these figures, and at the same time I am going to ask him to deal with the disposition which would be made of the surplus arising from the Madison operations for 1944 and 1945, and I think the suggestion will be made by him that the costs of the Hearing might very well be taken out of the surplus, after the Board has arrived at its decision, and then those costs will be eliminated from any further consideration.

Now, if Mr. Hamilton would be good enough to discuss this exhibit.

.....

ARGUMENT BY MR. HAMILTON

MR. HAMILTON: Mr.Chairman, with a view to getting the best approach to an understanding of these various exhibits, I think perhaps we should deal with the second sheet first, which includes the adjustment which we deem it proper to make in regard to the year 1944 for Madison, and the information that is here contained is based on M-9-A-44 actual, which is a statement filed by the Madison Company on the 1944 operations, but subject to certain adjustments which we consider are appropriately made.

In the first column we set out the total direct expense as given in the Madison submission, and those are the actual amounts expended in these various departments.

As has been explained before, however, the direct expense of, for example, the scrubbing plant, includes the costs transferred to the scrubbing plant of certain of the service units and the costs of those service units is inclusive of depreciation and rate of return and consquently to the extent that the Board might see fit to reduce the depreciation allowance and/or the rate of return, then the direct expense of the scrubbing plant would be in some measure overstated, and that applies to the total direct expense of all the operating departments.

We have not felt it necessary to indicate any adjustment to the depreciation charges made to the service departments, because in any event that amount is not significant, but we have made approximate adjustments to cure what appeared to us to be an excess earnings situation in the service units, which thereby results in additional direct

costs to the various operating units.

The first column then gives us the "Direct Expense".

The second column the "Administrative and General Expense", as shown by Madison in M-9-A-44 actual, with two adjustments: (1), to exclude that part of the administrative and general expense incurred by Madison in 1944, which was of a non-recurring nature, having to do with organization, preliminary organization and rate hearing costs, that amounts to $5100.00, and it was taken out for the purpose of uniformity because the corresponding amount in the next year is quite substantial.

The "Direct Depreciation" is set out in the third column and that represents the depreciation on the direct plants included in each of these various functions. The depreciation on the service units, as I have just mentioned, finds its way into the Direct Expense column or the first column of this sheet.

I might perhaps mention at this point that the adjusted rate base used for these utilities is $1,606,563.00, as set out in the footnote to the sheet.

As Mr. Blanchard mentioned a few moments ago, this relates to the submission in our statement W-H-7 of Exhibit 124, and has been adjusted by the amount of $905.00, being the approximate effect of the change in the field reserves as of December 31st, 1943.

The "Return on Capital" has been based upon the same ratebase plus an allowance for working capital in the amount of $140,000.00 less that portion of the working capital allowance which was utilized in the operation of the service units to the extent that the benefit of those service units goes to

outside parties.

The rate of return adopted was 11-2/3%.

The fifth column, the footnote is (c) and is an adjustment with respect to the approximate amount of excess return on service units which has found its way into the direct expense of those various departments and that adjustment is of course an approximate one but will be fairly close, I believe, and of course when I use the term "excess" it merely relates to the difference between the 15-5/6% return suggested by the Company and the 11-2/3% suggested by ourselves.

The next column is a charge for fuel in recognitione of a principle which Mr. Blanchard will no doubt be dealing with, and the amounts are taken from our original submission in Exhibit 124, on a basis of 2 cents for sour gas and 4 cents for scrubbed gas, with the revenue for scrubbing, compensation to the scrubbing plant, and that is indicated by the red figure in the amount of $4,335.00,, shown against the scrubbing plant.

The next column represents the absorbing of the service department losses and then we come to the sub-total representing the accumulated gross costs of all departments.

The next step is to transfer the compression costs to gathering and there is no problem of allocation in this year 1944 because there is no other function to which the charge could be made.

We then have the revised distribution of the total costs; and then that has been applied to the absorption plant or the dry gas purchases in accordance with the 60/40 split of gathering, with all other costs borne by the residue market.

On that basis the amount which would be charged to the absorption plant for the year 1944 would be $153,536.00, and that is based on a straight 60% or 40% of the total gathering and compression costs.

Now, Sir, Statement W-H-70-B, which next follows, is a similar presentation dealing with the year 1945, and I do not think I need to refer to it in detail, other than to say that it is prepared on substantially the same basis and is closely related to actuality, except for the adjustment to which attention is specifically directed in the footnote, it being based largely on the contents of M-9-A-45 actual as filed by the Company.

Statements W-H-70-"C", "D" and "E" relate to the years 1946, 1947 and 1948, and therefore to a greater extent are rested on certain assumptions which we have adopted pretty well from the original Madison submission M-9-A.

I perhaps should make this observation, Sir, that, although the inference seems clear, that the actual operating expenses are in excess of those originally estimated by the Madison Company, we have a substantial provision here for such an increase in costs, although it might not be sufficient. We have not taken out the twenty thousand contingent, or provision for contingent expenses, is the better way to express it perhaps, and we have also left in the administration the provision for rate hearing expenses, although that perhaps would not be necessary if the rate hearing expenses were otherwise to be dealt with.

I do not think it is important at this moment to deal with the total figures which result from this statement, because we will deal with those in summarized

form shortly.

Statements W-H-71, "A", "B", "C" and "D" are the comparable presentations with respect to the British American Oil Company.

Dealing with W-H-71 "A", the direct expense is given as from Exhibit 164, and likewise the administrative costs.

The depreciation, of course, is adjusted by reason of the change in the rate base and the basis of the rate base determination is given in footnote "C", where it is said that we allowed the high pressure lines and water stations at the adjusted historical costs plus 10% less accrued throughout depreciation.

We then allowed the whole of the 1944 expenditure at cost plus 5% for interest and head office overhead, and the 1945 construction allowed at cost for one half year.

I perhaps might explain why the change in percentage there. We thought that in allowing 5% for 1944 we would reach a result which was roughly comparable to the allowance of 10% in prior years, for the reason that a substantial part of what would normally be considered "overhead" has been charged up as a direct expenditure on the allocation and the additional 5% which we suggest may here be taken into account would be specifically for the provision of interest and head office overhead.

Of course when we get into 1945 the Company is in operation. Its administration costs are to be taken into operating expense and interest will be allowed by way of the rate of return and consequently no adjustment will there be necessary.

MR. HARVIE: Mr. Hamilton you have not the figure of the rate base arrived at there have you ?

MR. HAMILTON: I do not seem to have it handy. I can give it to you later if you like.

The rate base as of December 31st, 1944 was for new construction $636,462.00 and for the old installations $103,650.00. Those can be added together.

MR. HARVIE: And there would be working capital.

MR. HAMILTON: When we come to rate of return we have allocated at this stage only in the amount of $15,000.00 although we would be quite prepared to recognize an adjustment for an increase in the actual requirements for inventory purposes. I think Mr. Blanchard mentioned a few minutes ago that he had in mind $15,000.00 plus inventory. I think it was intended we would allow $15,000.00 plus the increase in the intended inventory.

The rate of return has been allowed at 11 2/3%. The cost of Madison's fuel has been allowed in approximately the amount of $1,000.00 and has been adopted from a previous submission Exhibit 124.

Passing on to column "F", the water station cost and the fuel scrubbing cost has been reallocated as on the basis suggested by the Company itself.

The compression costs are those allocated, the low and high pressure stations and then the revised total costs are split between the absorption plant and the dry gas

purchasers with the absorption plant paying 40% and the gas gathering, the dry gas market paying 60% of the gas gathering, and also of course the respressuring costs and transmission.

At the bottom of the final column in WH 71-A, we have deducted from the costs assessable to the dry gas market the amount of $11,320.00 which was recovered from Madison for the British American service charge in transporting G.& O. R. gas and also sundry has been deducted to arrive at the net cost of $188,000.00 which related to the dry gas delivered to the market worked out at 6.03 cents.

Now, sir, WH 71 -B-C and D are prepared on a comparable basis.

It might perhaps now -

MR. HARVIE: Using the same rate basis ?

MR. HAMILTON: Carrying it on through, yes. We might now turn to the statement on top of the set. Statement WH-69 which was the net result we had in mind in preparing the calculations on the sheets we have just been discussing.

This statement is intended to convey some idea of the approximate cost of gas disregarding by whom the money is spent but relating the expenditure to the gas that passes to market.

In the case of the British American the figures are shown at 1945 through to 1948. Likewise for the G. O. R. and for Madison we also include the year 1944.

At the bottom of the statement we indicate the approximate volume figures from which the unit costs were derived. The figure for 1944 and for 1945 is the actual one.

The market for 1946, 1947 and 1948 is related to a memorandum from Mr. Brownie, dated May 9, 1946,

plus further allowance of four hundred million for that part of the market his estimate did not seem to include, and I am speaking now of the Valley Gas Company and the Royalite Oil Company and such other minor customers.

The second section there deals with the total gross operating charges which are picked up from the statement we have just been discussing and the top part of the statement then results from the relating of those two factors.

It will be observed that for the year 1948 the average total cost amounted to 3.38 cents and that gas all came from the Madison system. I ignored the small amount of gas which passed from the British American in the last few days of the year. It did not seem to be significant.

That average cost increases in the year 1945 to 4.9 despite the fact that the total throughput is greater. The cost comes down slightly in 1946, goes up again in 1947 and again in 1948.

Mr. Blanchard mentioned that we had in mind that the Board might wish to express the allowance to Gas & Oil Refineries for gathering on the basis of something approximating a cent and in that connection it might perhaps be useful to give some idea of where the figure of one cent comes from.

The Madison cost for gathering gas for example runs on the order of a little less than two cents. The British American a little more than two cents. And, of that of course somewhat more than half is compressing cost which is not a problem of the Gas & Oil Refineries and that would bring you down to a gathering cost of about one cent. Added to that is the fact that the Gas & Oil Refineries being a smaller operation the cost would probably be a little higher.

If we tried to relate those to the operating expenses as shown for Gas & Oil Refineries gathering as given in Statement WH 68, making adjustments for additional depreciation, additional administration and return at 11.2/3% it would mean that the market would be bearing about 45% of the gathering costs and the absorption plant about 55%.

I think perhaps I should make an explanation with regard to the repressuring costs under the heading of British American because we show a repressuring cost of 1.685 for 1945. That unit cost of 1.685 is not the cost to repressure a MCF of gas in the British American area, but the cost per MCF that goes to the market of repressuring for gas which does not go to the market.

In connection with Gas & Oil Refineries we have a repressuring cost of .352 and for Madison of .196 and although this gas is both repressured at the same time the reason for the difference in the cost is that the portion of G. & O. R. gas which passes to market is much lower than in the case of Madison. It might perhaps be urged, sir, by some of the parties to this Hearing that the repressuring costs from all sources should be pooled and split, but that is not the view we adopt and not expressed in these calculations.

Mr. Steer was kind enough to point out to me a typographical error two-thirds of the way down in the Statement WH 69, where we say the estimated gross operating costs excluding 60% of gathering costs. It should be including 60%, excluding 40%.

If we can turn now to Statement WH 72; an attempt here is made to show what would be the cumulative earning position of the Madison Company if the suggestions contained

in Mr. Blanchard's argument and these submissions were adopted and the allocation of that excess earnings between the two customers, the absorption plant and the residue market.

In 1944 the Company actually charged the absorption plant $30,631.00 for its share of the gathering costs, but you will recall that subsequent submissions indicated that they would feel it proper for that charge to be increased to something on the order of $90,000.00, I think it is. But we left it just the way it was in the books so we would arrive at the net position for the absorption plant which shows that there is a deficit for the absorption plant of $74,000.00 relating to the 1944 operation.

On the other hand, the residue gas purchasers might look to the application of a surplus of $152,000.00 with the Company's net position being $77,000.00 over the suggested permissible earnings.

For 1945 the Company's overall position is that it failed to earn the suggested approximate rate of return of $22,000.00, but on - breaking that down between the two customers it becomes clear that on the basis of those assumptions the absorption plant is the one that occasioned the loss of $83,000.00 and there still remains on behalf of the residue purchasers $61,000.00.

Extending those two surpluses on behalf of the residue gas purchasers through 1946 and estimating that the change in price and so forth would be made effective approximately January 1st, 1947 the excess earnings on behalf of the dry market would be something on the order of threo hundred to four hundred thousand dollars after paying for additional rate cost .

I should mention that the rate hearing

expenses which were extracted from the administration costs in 1944 and in 1945 have been applied here as a reduction of the excess earnings and the cost has been apportioned between the absorption plant and the dry gas purchasers on the basis of the cost incurred on behalf of each.

The next Statement WH 73 merely sets out the similar situation with regard to the British American with a deficit of 1944 operations of $939.00. It is probably somewhat higher than that by reason of the exclusion of the rate of return, and for 1945 a loss of $106,000.00 of which $31,000.00 would be the deficit on the absorption plant, and $74,000.00 on the dry gas market.

You will observe the reference in the footnote to the effect that the deficit on the dry gas market is predicated on a provision for the payment of two cents on the gas which was split by the British American Oil Company to the British American Utilities. On the other hand it might be suggested that some part or all of that amount could be utilized to the reduction of this deficit.

THE CHAIRMAN: We will adjourn now.

(Go to Page 7279)

2 P.M.SESSION

MR. BLANCHARD: Mr.Chairman, I will now refer to the summary, page 1, of Exhibit 194, and you will have observed the very wide disparity between Madison on the one hand and British American and Gas & Oil Refineries on the other, in delivering gas to the Gas Company's gate on the basic rate basis and the cost allocations set forth in the exhibit.

In 1945 the cost of bringing gas from British American to the Gas Company's gate is a difference of 4 cents; 1946, 4.5 cents; 1947, 4.7 cents; and in 1948, 5.2 cents.

Now, you are directed to fix a fair price for dry gas at the well head, and when one comes to compare these figures one wonders how a uniform price can be paid throughout the whole field, unless the producers served by Madison are going to very substantially subsidize the South end of the field.

Now, I might just refer also to the average total costs which are rather encouraging. The average costs are 3.38 in 1944; 4.92 in 1945; 4.88 in 1946; 5.17 in 1947; and 5.58 in 1948. And if all the producers in the field are perfectly agreeable that they should receive the same well head price, there would not be the problem that is presented here.

Now, from an early point in these proceedings, at least the point at which we reached the question of the allocation of costs, I have always been impressed with the fact that the proportion of gathering costs to be borne by the absorption plant was not the amount of gas actually lost in the process of absorption, but with the utilities performing a service to the absorption plant, and I have indicated that, I

think, a number of times in cross-examination of various witnesses, so that to me it is not a new thought at all. In other words, the gas that comes through to the absorption plant, every foot of it, is used by the absorption plants as my friend, Mr. Steer, very clearly pointed out. That gas, every foot of it, carries those hydrocarbons that the absorption plant needs, so that every foot of that gas is performing a service for the absorption plant and the absorption plant can take out of the gas such hydrocarbons as the absorption plant pleases. No one else can say to them "You must process for a 45 pound product or a 26 pound product; you must leave so many B.T.U.s in our gas." No one has anything to say about that except the absorption plant. And so I say, and I think it is sound, that the absorption plant should pay on the very simple formula evolved by Mr. Steer, assuming 15% loss to the absorption plant, then that the absorption should bear $\frac{100}{185}$, because there has been a service performed with regard to every foot of gas that goes into the absorption plant, and if there were no natural gas marketed, it would be flared, and so far as the absorption plant goes, so far as the use of the gas goes, it might just as well have burned it all. It is finished.

Now, it seems to me that is a more correct and a much simpler formula than the formulae which were prepared by my friend, Mr. McDonald, and my friend, Mr. Harvie, and which, I confess, I could not understand, and so I called in Mr. Hamilton and we spent last Saturday endeavouring to see whether there was any scientific basis for the application of the formula as between an absorption plant and the gathering lines, and I am happy to say that Mr. Hamilton was equally puzzled to find one, and my submission is that there is no formula based on Mr.

Zinder's proposition that can be applied. It seems to me that the fact is that the absorption plant is using all that gas, and after they are through, we get some of it, that is, the utilities get some of it, and that the proper formula is the one Mr.Steer proposed. The difficulty about that formula, however, is that it cannot remain constant.

For instance, when the North return fuel line goes out of the picture, your fractions change, and the same is true if by some process less gas is lost in the other absorption plants. So that Mr.Steer, I suppose, having that in mind, has suggested a 50-50 per cent allocation, and it seems to me that that is a fair allocation and that it is an extremely generous one. I hope I am not exaggerating, but that is the view that I want to express. So that in presenting Exhibit 194, Sir, I do not want to be bound by it in anyway as to the allocation of costs.

Then what is to be done about this differential between the North and the South ends, and between the North and the Gas & Oil Refineries? In the early stages of this Inquiry, that is when this Board was holding hearings for the purpose of deciding what would be done about conservation in the South End, to what extent it would be carried, and whether or not the B.A. proposal would be accepted, my understanding is that Mr. McCutchin, and I think Mr. Harvie, also, said that after making an estimate of the costs of the low pressure system, $480,000.00, said that they would bring gas to the Gas Company's gate at the 7¾ cents, including, and my learned friends will correct me if I am wrong, including the 2 cents at that time to which the producer was entitled.

MR.HARVIE: That was wrong.

MR.BLANCHARD: That may be wrong. In any event, that

you would look after the producers out of the 7¾ cents, am I correct about that?

MR. HARVIE: No.

THE CHAIRMAN: The only qualification I remember was subject to a reasonable price for scrubbing.

MR.BLANCHARD: That may be so. I have Mr. McCutchin's statement before me. I do not want to misquote.

MR. HARVIE: I think that is right as you suggested, Mr.Chairman.

THE CHAIRMAN: Subject to a reasonable scrubbing cost.

MR. CHAMBERS: Mr. McDonald put it on the record.

MR.HARVIE: And subject to the producers and the B.A. Utilities being free to negotiate new forms of contracts, or anything else they wish.

THE CHAIRMAN: And above all the B.A. would take the risk of losses.

MR.BLANCHARD: Yes. And there was an estimate, I think, by Mr. McCutchin of 5.4 cents downstream the scrubber. I think I am correct in that. That is my impression.

MR. McDONALD: Upstream.

MR.BLANCHARD: Yes, going into the scrubber,

MR.HARVIE: 6½ cents, I think it was.

MR.BLANCHARD: Now, on page 1 of Exhibit 194, we have these prices: 7.8 cents in 1945; 8.21 in 1946; 8.78 in 1947; and 9.68 in 1948. The gas from the Gas & Oil Refineries is, of course, higher still.

Now, my submission, Sir, is that the estimates which were given to this Board in the early Hearing to induce this Board to adopt the scheme of the British American, much to the extent that they are in excess of, they

must be reduced. It seems to me, Sir, that if the producers in the South End are to enjoy any benefits whatever from the well head price, the cost of taking the gas to the gate of the Canadian Western must be reduced.

My suggestion, Sir, is this, that the rate base to be allowed to the B.A. so far as the low pressure system and the installations are concerned, should be the amount of the estimates made by Mr. McCutchin, plus the, I think the $45,000.00, in that neighbourhood, authorized by the Board, plus the amount paid under the Gentry Contract plus 10% overhead.

THE CHAIRMAN: If you put it that way, Mr. Blanchard, you would have to deduct from the original estimates the amount which they had estimated for laying the lines which the Gentry Company did.

MR. BLANCHARD: Now, I have not the figure before me, but I think the amount by which the Gentry Contract - well perhaps the old contract, was seventy-seven thousand dollars something.

MR. HARVIE: That is the excess.

MR. BLANCHARD: That is what I understood, that is the excess, $77,000.00, and that that should be allowed.

Now, if that is done, and the gathering costs, as I have suggested as between the absorption and the utility is divided 50-50, it will result in a lower cost to that, a fairly substantial lower cost, in bringing that gas to the Gas Company's gate.

Even then the question of the differential as related to the well head price is a difficult one. One might take the view that until the rate base has been amortized that the producer in the South End would not get

anything. I am not in accord with that, for this reason; I think there must be some well head price paid to the producers in the South to keep their wells in operation as the pressure goes down and that there should be some payment to the producers in the South End and in the G.O.P. end. I do not think there is any scientific way of allocating that. I have tried to think of one, but I have not been able to, and it seems to me it will have to be a pragmatic adjustment in some way. Certainly the North End should not subsidize the South to the full extent that would happen if there were a uniform field price.

THE CHAIRMAN: Of course, if the Madison "A" Plan had been put in, that would not have included the low pressure system or the B.A.

MR.BLANCHARD: No, if the Madison "A" had been put in, that would not have included the low pressure system of the B.A.

THE CHAIRMAN: And then it would be a unit operation and there would be no question of one part of the field subsidizing the other, because what would have happened is that the compression would have been needed at the B.A. absorption plant.

MR.BLANCHARD: I have not considered that.

THE CHAIRMAN: And the residue gas line would have been needed to go to the scrubber. This gas would have gone in in any event and it would mean a unit operation, and there would be no question of subsidy that may arise with the low pressure system there.

MR.BLANCHARD: Yes, it is the low pressure system that has created the difficulty, and that low pressure system was installed on the basis of certain estimates that were submitted to this Board.

Now, as to the well head price, Sir, I

disagree with my learned friend, Mr. Fenerty, that the gas has not a commodity value at the well, that is, if it can reach the market where it is needed, and I think the answers of Mr. Zinder given on pages 4228 and 4229, Volume 54, dealt with that very clearly.

In any event, you have been directed to fix what is a fair well head price, and again it seems to me that there is, unless you take the competitive fuel evidence and apply it here, and say there is so much cushion between the cost of getting the gas to the burner tip and the competitive fuel price, unless you take that as a guide there is nothing really to go on.

Now, it seems to me that there is probably room between the costs, including the Gas Company's costs, and the competitive fuel costs, to allow a fair price to the producer. But it also seems to me that it would be extremely unwise to assume without the evidence, of course, that the Gas Company is making any surplus profits on its allowed rate of return at the present time, and it would seem to me a great mistake to allow a well head price on the basis of all the traffic will bear.

(Go to page 7386)

I think that the limit upwards should be 4 cents and possibly that 3 cents would be a fair allowance under the circumstances.

MR. McDONALD: On what price, in the consumers' price or the price to the Gas Company?

MR. BLANCHARD: I am speaking of the price to the producer.

THE CHAIRMAN: At the well-head?

MR. BLANCHARD: At the well-head, yes. That is what I am speaking of. Now the Gas Company's rate was reduced 2 cents in the last rate fixing.

THE CHAIRMAN: 1943.

MR. BLANCHARD: Yes sir. And it seems to me that even if the allowance of say 4 cents price resulted in the Company having to reinstate the previous rate that it would not affect the market to the degree feared by my friend Mr. Fenerty. So that my submission is based on the figures that we have in Exhibit 194, that there is room for a 4 cent rate if this Board inclines to fix that amount within the boundaries of the old domestic and commercial rate in Calgary.

My suggestion, sir, is this that so far as the Producers in the South End are concerned they will have to be paid on a pragmatic basis, say one-third to one-half of the well-head price fixed for the North End. The average then, sir, might mean a higher amount than 4 cents to those in the North End of course but I am not certain how that will work out. As to the Gas & Oil Refineries it seems to me there again that some price will have to be paid to the Producers in that area, notwithstanding the cost of getting their gas to the market, as an incentive to keep the wells in operation. I think that might have a definite effect in

that direction. We have unfortunately before us no figures to show to what extent a 1 or 2 cent rate would assist the Producer whose wells, crude wells have got to the point where it does not pay them to operate them, to what extent the 2 cent rate for gas would assist them to make it worth their while to continue to operate. That is something I think the Board will have to take into consideration.

THE CHAIRMAN: If your premises are sound, Mr. Blanchard, would not the proper way be to fix a uniform well-head price for the field and deal with the differences in the various parts of the field by cost allocation. Would that be a method whereby it could be done?

MR. BLANCHARD: Just where is the foundation for the cost allocation?

THE CHAIRMAN: What I have in mind is this, supposing we fix the British American rate base at X Dollars.

MR. BLANCHARD: Yes.

THE CHAIRMAN: And then we say the cost of operation, which means direct operating cost, depreciation, management and all that sort of thing, is to be charged only as to the fraction thereof against the dry gas and the rest by British American or the G.O.P. Company according to agreement between themselves and the Producers, their own company.

MR. BLANCHARd: It might be reached on that basis.

THE CHAIRMAN: Would that be in order, Mr. Hamilton?

MR. HAMILTON: It might be worked out, sir, yes.

THE CHAIRMAN: I mean if I come to the conclusion that something of that kind should be done?

MR. HAMILTON: Yes, sir.

THE CHAIRMAN: I am only thinking out loud at the moment.

MR. BLANCHARD: What I had in mind, sir, was on these figures as they stand in 194, it would be improbable that the producer in the South End would be entitled to payment of anything at the present time without raising the price of gas altogether too high. At the same time, as I say, I think there should be a well-head price paid in the South End and in the Gas & Oil Refineries' zone for the purpose as I have said of keeping them on operating these wells. With reference to the allocation of costs, sir, between the absorption plant and the utilities I would like to remind the Board of a statement made by Mr. Teis at page 2871 which seemed to me to be some authority for the position that I have taken, and Mr. Steer has taken, when he says that the division of costs between the absorption plant and the utility should be based on the relative utility in the system to the particular use.

MR. CHAMBERS: What page, Mr. Blanchard?

MR. BLANCHARD: That is at page 2871, Mr. Chambers. I think that when he made that answer he had in mind precisely the factors that I have mentioned, sir, as applying to the allocation of the division of costs between the absorption plants and the utilities. I do not think, sir, there is anything more I have to say.

I should have said, sir, I overlooked the matter of the high pressure lines when I was speaking of the rate base of the British American and I would suggest, sir, that they go into the rate base at historical costs less accrued depreciation, throughput depreciation, notwithstanding that the Board was assured, at least I think the Board could assume that they had been assured that those

lines were not coming into the rate base at all. And the explanation is of Mr. McCutchin and no doubt that is the explanation that Mr. McCutchin thought they were not going into it as a public utility upstream the absorption plant. But at the same time if that was his idea, he did not suggest the British American was going to make any charge for bringing the high pressure gas upstream the absorption plant.

MR. HARVIE: He did suggest though that there would be a downstream absorption price that would look after that.

MR. BLANCHARD: I have no recollection of that evidence at that time, Mr. Harvie. I have no recollection of such evidence.

THE CHAIRMAN: Well, gentlemen, you have all had your say. As I mentioned yesterday, I noticed that a few of you were busy with pencils and I assume that you have something to say in reply to one another. I suggest we start off, if you have a reply, that we start off in the original order. Mr. Chambers.

MR. CHAMBERS: Thank you.

THE CHAIRMAN: And without suggesting that you limit yourselves too much, we have ended two weeks of the most intense constructive and destructive argument that one could possibly have out of 81 volumes of evidence.

MR. CHAMBERS: I can assure you, sir, that everyone here - I am speaking for myself in particular - is as anxious to conclude as you are, sir.

I had, of course, directed my attention particularly to what had been said up to yesterday. I have made notes of certain matters that my friend Mr. Blanchard

raised this morning. Of some of them, of course, we were entirely ignorant for reasons that are apparent. Representing the Government as he cross-examined, he sounded all theories. Others of us who were present made our position probably clear during the course of cross-examination. But the point I am getting at is this that I will endeavour to follow the notes that I made concerning some suggestions raised by Mr. Blanchard and argue them and work them in with the other as I go along, and if I take a little time in checking those, I give that as a reason, sir.

I think we all recognize first of all that the basic thing that your Board has to fix as one of its main starting points is this rate base. All of the counsel have directed their attention to it. The ideas have not been uniform which is to be expected. But I do think from the statements of counsel that we all recognize that in the first instance what your Board is to seek is a fair value of the property. Now we may have, and obviously have, different ideas as to how you should arrive at that value.

THE CHAIRMAN: At the moment, the score is 3 to 3.

MR. CHAMBERS: But under the Act, Section 49(1), and it has been in our utilities . . . . . In this Act and in the Public Utility Act, I think for the last 30 years, that the Board shall appraise and value . . . . .

MR. STEER: "May".

MR. CHAMBERS: "May", yes and my submission, for the reason I brought out in the opening of my argument, is the word "may" means "shall" under circumstances such as this.

THE CHAIRMAN: I think "May" simply means if I do not want to do it I do not have to, but if I get to a rate base

I must.

MR. CHAMBERS: That is it. Now I suggest, sir, that hitherto, up to the time that this Act was passed, that the regulatory Boards in the Province, and I am referring to the Public Utility Board itself and also to the McGillivray Commission, whose finding was passed and ratified by Order-in-Council and then by virtue of the statute became an Order of the Board of Public Utilities, have in instituting regulation used as a basis of fair value either of two things. First of all, Reproduction Costs New less Depreciation of some kind. In the Red Deer case, to which my friend Mr. Steer referred the other day and in the McGillivray Commission and with respect to the Valley Pipeline the cost has been prudent investment and depreciation. In the 1920 case, sir, and I suggest that these are all the precedents we have in this Province and I am regarding as besides the point the instances where utilities have been set up anew with the Board's approval under a certain set of conditions,

(Go to page 7392.)

Now the reason I mention that is this, that these two things that I mentioned are factors in the expectation and planning of profits.

Now in the 1921 Order of the P. U. Board and I referred to it in my argument and my friend Mr. Steer referred to it, and I submit on your reading of that judgment you can come to no other conclusion but that the Board had before it two diametrically opposed contentions; one was the Company argued for reproduction costs new less observed depreciation and the City contended for original costs. The Board, definitely, in that particular case did not adopt reproduction costs new but prudent investment so those cases to all intents and purposes are what Mr. Hamilton recommends here and then the Board used these very significant words, and I am referring to this fact also, that in 1921, a period of high prices, that in view of the condition of the plant and its being well maintained and a few of the methods of arriving at the rate base, which could mean nothing else I submit on the reading of that judgment, they took prudent investment and they were not going to depreciate it.

Now, sir, I suggest that the Public Utility Board did not do that without reason and that the cases in the texts which I have cited to you in my argument at Page 6301 show that there were precedents for doing that, and many decisions in the United States even today, not all of them by any means, say if you take that kind of a rate base in the first instance it should not be depreciated.

Now both Mr. Steer and Mr. Fenerty have contended to you, sir, that the House of Lords Cases and the Court of Appeal Cases which I quoted at some length to you in

my opening in support of the reproduction costs new, less depreciation as a test of fair value, were totally inapplicable here and that they should not be given any weight to as they were condemnation cases.

Now you will recall that I referred to, I think it was the Edinburgh Case and the London County Council case and the Toronto Railway and the Melbourne Case and also the International Railways Case. Now I would point this out to you, sir, that in each and every one of those cases the valuation, or the fair value, that was being sought was done under and pursuant to the terms of the Statute that was enacted before the particular undertaking was in creation. In every one of those cases the Company was incorporated by a special Statute and under the terms of that special Statute there was incorporated into it the terms of those Statutes, - some of them were Statutory agreements but I am referring particularly to the Edinburgh Case and the London County Council Case, that those Companies, having obtained their statute of incorporation and having ascertained the rules under which they were going to own and operate and lose control of or sell the property, - those things were laid down before they started, and they took the plant and operated it in accordance with those conditions and I say that they were not condemnation cases in this sense, that they were cases where the Company started out on an undertaking and as a term of its institution they gave an option as part of the conditions under which they operated to an outside party, at a stated time in the future, to acquire the property on the basis of a fair valuation to be fixed by some outside party and now, and I suggest this very emphatically, that in the Edinburgh cases and in the others too, the Acts which

governed were the Tramways Acts of 1870, Chapter 78, and it still is the law in England, and the Act of Incorporation as I said, incorporated Parts 2 and 3 of that Act into the Company's Charter and into its powers and Section 43 of that Act said: One of the conditions is that at the end of 21 years, - we are going to grant an option that at the end of 21 years the municipality may acquire the property at its then fair value, at its fair value.

THE CHAIRMAN: That is compulsory purchase, I suppose, instead of appropriation, it is compulsory purchase.

MR. CHAMBERS: No, as I recall, sir, the municipality did not have to exercise the right.

THE CHAIRMAN: No, but they had the right.

MR. CHAMBERS: Oh, they had the right.

THE CHAIRMAN: Of compulsory purchase.

MR. CHAMBERS: Oh certainly.

THE CHAIRMAN: As we have under our Act.

MR. CHAMBERS: Yes, but the undertaking did not have to operate. It went into it, the owner went into it with his eyes open before he invested his money he knew that at the end of 21 years that property would cease to be his under certain conditions.

THE CHAIRM'N: Then is not the principle laid down, and I think it is in the Chesterfield Waterworks case, very clearly laid down, that in the case of compulsory purchase, the purchase price shall be the value of the property to the person from whom it is being taken and is there not some slight difference between that and a case of something for which you are going to make a rate of return.

MR. CHAMBERS: I say in connection with that, there is

this difference, that we cannot get a valuation based on any profit made and I do say that in these cases to which I referred the statute expressly made it clear that that was not to be taken into consideration.

MR. CHAIRMAN: Quite so.

MR. CHAMBERS: And I say that the ordinary decision in those two kinds of cases is the very thing you can put your finger on, but in the cases I refer to, the statute was very careful to say that that was not any part of the valuation, and here is another interesting thing, sir, that in that Tranways Statute and the other statute, there was a provision that the undertaking's rates should be regulated. They were under regulation. True, not the same kind of regulation we have here. In England they adopted another principle and the statute said they must charge "reasonable rates" and the Board of Trade had certain jurisdiction . . . . .

THE CHAIRMAN: Which is a department of the Government.

MR. CHAMBERS: Yes, but it is the over-all principle which England has adopted, instead of adopting the American one of regulation, in other words, the point I am making is this, that these cases are similar to this extent that even when you expect or might expect your property is going to be controlled by somebody else, or you are going to lose it altogether, and even although in the meantime you are not free to make every dollar you like, that when the time comes for the valuation, that reproduction costs enter into the picture. Now I never contended that reproduction costs new less depreciation is the only element or matter to be considered by your Board here but I say that it is an important element that must be taken into consideration and given great

weight too, especially in a period where the prices are not the same as at the time of construction.

Now then I say that the condemnation cases, knowing full well the rules under which they operate, they are in a different class altogether and the courts and the statutes have recognized that there has to be some or should be some special allowance for interfering with profits of the business and for compulsory taking.

Now then I also point out this that in the International Railway case, which went before the Privy Council in 1937, it was not even a case of compulsory purchase..

THE CHAIRMAN: It was a contract.

MR. CHAMBERS: Yes, and even under the statutory contract, which I say is exactly the same as the Tramways cases, but under that contract, which was a part of the statute, the Company had the right to transfer, whether or not the purchaser wanted to take it and in that particular case the purchaser did not want it at any price other than for scrap, that even under those circumstances the highest court of this country said that reproduction costs, when you are talking about value, that it is an important element and in that case they said it was important.

THE CHAIRMAN: I have not read that case for some years, Mr. Chambers, but it is my recollection that Lord MacMillan, in laying down the reproduction costs new theory, even in that case, mentioned that different circumstances might apply if depreciation had been recovered through the charges made by the railway companies to the public, and he said it in much fewer words that I have expressed it in now, but I have a memory of something like that being said in that connection.

MR. CHAMBERS: I remember you mentioning that in another case and I think there is no doubt that he referred to "depreciation" but I remember too, and following that, I had occasion to go through the report of the cases in the court below and they referred to the fact that the company had not, in the last year or two, earned enough to pay depreciation and other costs. Now what took place before that I do not know.

THE CHAIRMAN: Do you recollect that, Mr. Steer.

MR. STEER: No, I do not, I must say, sir, but I would like my learned friend to indicate on what principle depreciation has to be ignored because the historical costs basis is adopted? I have heard nothing to indicate anything like that.

THE CHAIRMAN: There is nothing in the evidence unless you can say that it is a principle which has been developed in public utility cases.

MR. STEER: Then if it is a principle of law it must be laid down as a principle, and what is it?

(Go to page 7398)

I will go further in a moment but I say this it is true that historical cost as such in itself is not any evidence of value at all, but I say if the Tribunal decides having regard to all the circumstances that we are going to take then in fairness we at least are entitled in accordance with practice in this Province to the benefit of the precedent and practice that the Board followed in another case.

THE CHAIRMAN: As a matter of fact, Mr. Chambers, I think there was a decision of the Board when they held that the method of appraising the value was different in the case of fixing rates as against fixing a price for compulsory purchase and that is in the Wainwright case which is not reported.

MR. CHAMBERS: And that Wainwright case is reported, the Court of Appeal that is.

THE CHAIRMAN: No, no, the decision of the Board of Public Utilities Commissioners. Do you remember that Mr. Fenerty. You know something about that one, do you. Do you remember if the Board of Public Utilities Commissioners held in the Wainwright case the principles of valuing for rate base purposes were quite different from those to be used in fixing a price for compulsory purchase ?

MR. FENERTY: No question about that.

THE CHAIRMAN: I thought there was that decision.

MR. FENERTY: They certainly held that the principles for compulsory taking, in the Wainwright case, recognized as the value to the party and they went the whole way and pointed out the entire distinction involving the different purposes of the approach. I think that is right.

THE CHAIRMAN: And that is a decision that must be ten

years ago I think.

MR. CHAMBERS: Probably there is another Wainwright case, I am referring to.

THE CHAIRMAN: The one that you have in mind, Mr. Chambers arose out of that decision of the Board.

MR. CHAMBERS: Oh I see, but that in that decision of the Board you will recall that turned on this ground after the Public Utility Act was passed. There were certain undertakings and they thought that the Wainwright was a good place to put in a gas undertaking. They went to the Public Utility Board before they built anything and they gave the Public Utility Board an estimate of what it would cost and the Board in that case said all right we will approve your franchise at certain rates and the Board wrote a letter saying this is all conditional on your estimate as to cost.

THE CHAIRMAN: Quite right.

MR. CHAMBERS: And you will remember the first hearing came on. You will remember they had been going some five or six years after the plant had been built and the evidence disclosed that the capital cost was not as much as they had estimated to the Board.

THE CHAIRMAN: And then ten years later, Mr. Chambers, ten years after that decision the town decided to exercise its right of compulsory purchase and an application was made to the Board to fix a value and it was in fixing the value of these properties that the Board laid down, and I am quite sure I am right, that there was a marked distinction between the basis on which you made a valuation for rate making purposes and for compulsory purchase.

MR. CHAMBERS: But I do say this, sir, that the Board,

the Board of Public Utilities has said in this Province it is either one or the other and it is the only two ways they have applied so far.

THE CHAIRMAN: And the Board has also said it is not bound by its own decisions.

MR. CHAMBERS: Yes. I am quoting it for the purposes of meeting and dealing with this argument that we expected this was going to happen and I think this element of expectation is a very important one for the basic reason that we discussed with Professor Stewart in the best interests of everybody in the long run that people know a certain procedure is to be followed unless of course the Legislature steps in.

THE CHAIRMAN: Well I have interrupted you too much Mr. Chambers and I will try to keep quiet.

MR. CHAMBERS: No, that is all right. As long as you do not hold to a time limit, sir.

Now then, sir, a lot has been said about this Section 49 (2) having changed everything and that you do not have to bother about the ordinary principles of fair value.

Now, sir, I would like to read that sub-section again. Now the sub-section says this in fixing and determining price for value and of any real or personal property for any of the purposes of this Act, the Board shall not be bound by the price paid or the replacement cost or any book values however established by the owner for such property.

Now my learned friends, at least some of them, tried to read into those words the theory that the Legislature has pointed out to your Board reproduction cost is not in the picture.

I suggest that the Legislature in those

words has put the whole thing in the same boat. That you are not bound, you are not necessarily bound by book cost, what price the owner paid, which is another way of saying cost, or by reproduction cost.

THE CHAIRMAN: It is purely a negative provision.

MR. CHAMBERS: But you may do this, adopt any basis or formula which to it shall appear just and reasonable.

Now I suggest down to that point at least, that is all they did mention about value of security and so on, but the Court in interpreting that last one, it boiled down to that there was no single formula. That is what the Supreme Court said in effect I submit from 1893 down to 1942 I think it was. And I say that down to that point the Section is in effect putting on paper what the Utility Board and the other Boards of this Province have done down to that time.

Now then one other point and in particular and without prescripting the generality of the foregoing the Board in fixing such price or prices or values shall determine the just and reasonable allowance for depreciation.

Now the Board has to do it. Not some Company by the way it enters up in its books. "And the Board in so determining a just depreciation" may what, take into account depreciation already taken. That is one of the factors undoubtedly your Board has a right to do. Take into consideration. There is no mandate there that you are to be bound by the amount of depreciation entered in the books.

And I submit that that section as I stated in my opening argument is designed to cover every rate hearing case even companies that build their undertakings under rate base.

Now I suggest, sir that in the English Statutes

and cases which I have cited nothing is to be allowed for compulsory taking or the loss of profits and in that way they are authority for circumstances such as these. I am assuming that these Companies who are now being regulated and whose rate bases are being fixed have some expectations that some day they would come to a proceeding something like this, but I do say that in the light of law or the principles of fair values from the time it has been enunciated by the Courts of this country and of the Old Country and even in the United States and the principles of valuation as applied by the Public Utilities Board here has as a legitimate part of their expectations the right to assume and to know that when they were spending their money and developing the field that when the time came, if ever, for your Board to fix a fair value that one of the items and important items to be given consideration to and I do not mean consideration merely for the purpose of looking at it, and going into book costs or adjusted historical costs.

Now finally my learned friends also say and I am referring particularly to Mr. Steer and to Mr. Fenerty, that irrespective of what Section 49 (2) says or irrespective of what Section 49 (1) says that by reason of the one or two recent decisions in the United States the picture has changed and they referred to the Natural Gas Pipeline Company of America in 42 P. U. R. and also to the Hope case.

Now I would point out there the Commission's mandate in the Statute was actual legitimate cost and that is what the Commission was finding, not value. It was not intended to find value and they were not necessarily out to find reasonable rates in the sense of just and reasonable. They had a

mandate if they wanted to, to fix and arrive at the lowest reasonable rate.

MR. STEER: They were to find the actual legitimate cost. It was a discretionary thing, the Statute simply said the Board may.

MR. CHAMBERS: And I say here they are. It says the Board may appraise and value, and that is a fine distinction between the two Statutes.

Finally Mr. Steer, and I may refer you to Page 7175 of his argument where he says that because Mr. Justice Black of the United States Supreme Court in his reasons in the Natural Gas Pipeline case of 1942 states of himself, not all the Court, and two other Judges, because the opinion of the Court was delivered by Mr. Justice Stone, although Mr. Justice Black agreed in the result, but what I am coming to is this statement relied upon by Mr. Steer and quoted by him, of Mr. Justice Black, which is not necessarily the view of the entire Court and this is what Mr. Justice Black said. It is quoted in part by Mr. Steer at Page 7175 from Page 147 of the report.

(Go to Page 7404)

At page 147 of the Report, we have, where the three Judges say "This is an appropriate occasion to lay the ghost of Smyth & Ames which has haunted the utility regulations since 1898."

Now, as I understand it, the argument he advanced by reason of that statement by the United States Supreme Court, or of some of the Judges, that we should turn over and lay down a new set of rules in this country merely because of a certain statute that has been passed in the United States or a certain policy has been adopted by the United States Supreme Court.

THE CHAIRMAN: I wonder if you could put it this way, Mr. Chambers, perhaps, that the decision in the Hope case was simply the culmination of a trend that had been growing up over a number of years.

MR. CHAMBERS: That is the point I am coming to. I say it is implementing the New Deal in the United States. Now, it is common knowledge and it is in the Press, and they talk about it down there in a sense that we never talk about it here, of putting certain people on the Courts because they hold certain views, and we would never think of it, and it has never been heard of in this country. And the result is that there are certain people appointed to the Courts of the United States because they favour the New Deal. That might be all right, but I say that we necessarily do not have to adopt the New Deal because certain of the United States Judges decide to do it that way by reversing the decisions of the Courts.

THE CHAIRMAN: And most of them changed their opinions after being appointed to the Bench for a while because they decide that they are lawyers first and politicians second.

MR. CHAMBERS: I submit that some of them have not

yet decided that they were lawyers first and politicians second by something that appeared in the Press within the last cew days, with regard to some of the Judges, and Mr. Justice Black is one of them.

Now, I am urging on you, Sir, that in the costs of, not only the parties that happen to be before you on this occasion, I mean in the interests of not only the parties that happen to be before you on this occasion, but in the interests of regulation generally, that some semblance of precedence should be followed, and that we in this Province should be entitled to rely on and expect from the regulatory Boards, that they will follow the fundamental princi les of valuation that have been laid down from time to time by the Courts and applied by the tribunals, and that by reason of what has happened in the United States, and by reason of the wording of Section 49(2) there is no occasion at this moment at least to turn over a new leaf.

Now, there is a case which I am just going to refer very briefly to, or rather there is a matter to which I am going to refer very briefly, and that is the matter of going value.

MR. STEER: Now, Mr. Chairman, if I may interrupt my learned friend, I have the passage which I think you wanted, Mr. Chairman, and perhaps I will just mention it to you so that you may refer to it, and that passage is found in the International Railway Company case, in 1937, All England Reports, at page 188, and it reads this way:-

> "If the terms of transfer rightly construed 'may' entitle the company only to the break-up value of its railway at the termination of its franchise, sound accounting would have indicated the propriety

"of building up an amortisation fund out of earnings during the currency of the franchise."

THE CHAIRMAN: Yes.

MR. STEER:

"It is at least questionable whether, under the last article in the agreement, requiring the imposition of reasonable passenger fares only, the parks commissioners would have approved of the cost of such a fund being represented in the fares."

THE CHAIRMAN: That is the passage I had in mind.

MR. CHAMBERS: But I do say this, Sir, all that the Judge said there was it is questionable whether the parks commissioners would have agreed to it.

THE CHAIRMAN: I know, but there was a clear indication to me at least that different principles might apply if it could have been established that the prices charged to the public included an amount which would be used for amortization.

MR. CHAMBERS: I do not think there is any doubt about that.

THE CHAIRMAN: That is the implication as I take it.

MR. CHAMBERS: And then as against that I say that that case is certainly extreme in the other direction too.

THE CHAIRMAN: Oh yes.

MR. CHAMBERS: You have a plant and equipment that never can make any money.

THE CHAIRMAN: I am sure it was a great shock to the parks commissioners.

MR. CHAMBERS: Now, I just want to refer for a moment to the fact that my learned friend, Mr. Steer, claims that going value is a matter of costs and not of value at all. I agree,

of course, that it a matter of costs, but it is a matter of costs whether it is reproduction cost new or whether it is historical costs or original costs, and that if it is an element of cost, it is also an element of value.

And then you, I think, Sir, were inquiring about whether it was in the Public Utility Reports, and for the purposes of the record, the case I referred to is the United Gas Public Service v. Texas, 1938, 22 Public Utility Reports, New Series, and Chief Justice Hughes of the United States Supreme Court certainly says it is a matter of values. I read that before, but I will read it now:

> "That by 'going value' was meant the added value of the appellant's property as a whole, used and useful for serving the city, over the sum of the value of its component parts."

and so on.

So I say that your Board, Sir, should consider that reproduction cost new less depreciation is one of the important bases upon which you should fix the rate base, and that the mere fact that you adopt reproduction costs does not necessarily mean that going value should not be in the picture.

Now, true, I will admit that from the standpoint of actual costs as to what money was spent in the interests of going value, or for the purposes of going value, there is no specific evidence in this case, and there is a perfectly good reason for that. We would be all surprised if we should find the exact dollar entries in the books of this company to show the specific items to bring about as to what is now claimed to be an item of going value. But there is some evidence of money spent to condition or to bring the

plant to its working condition. Mr. Hamilton mentioned that in connection with the installations of the Girbotol royalty. There is a new system up-to-date, but it had to have certain adjustments, and certain moneys were spent that were not recovered in adopting that new system to the conditions in this country.

And then on top of that so far as reproduction cost new was concerned, and I submit it is just as applicable to a valuation of a rate base on the basis of historical costs, is the evidence of Mr. Hill who says over and above the valuation that "I have placed on this property, I am satisfied there is still an additional value of $200,000.00" and he gives the reasons for it.

Now, I submit,Sir, that we are entitled to believe Mr. Hill to this extent that the bases upon which he placed that amount are there. Now, whether or not he has taken the right amount, or whether or not you should adopt that amount, or more or less, that is a matter for you, sir. But I say the fundamentals are there upon which you can arrive at the judgment. And I do submit that in view of the evidence, and in view of some of the arguments of Counsel here, Mr. Hill's evidence is corroborated to this extent, that this company and the people that designed its property, and brought it into working condition, knew what they were about.

Now, another point. My friend, Mr. Fenerty, says that there is now no evidence before your Board, Sir, as to the present, and I gather that he means today, reproduction costs, as Mr. Stanley Davies had given some evidence to the effect that the Dominion Government has removed the 8% sales tax on certain things. Now, in answer to that, I would say this, in the first place that Mr.Davies did not

know what he was talking about, if, and I am not saying that he intended it, if he meant to convey to your Board that present-day values of materials of the nature of those that are in the systems are now 8% less by reason of that tax removal, and the reason I say that is this, Sir, that Mr. Hill's subsequent evidence shows that is not so, that he has made certain inquiries that that 8% tax having been taken off, was more than offset by other things that followed, the removal of ceilings and so on, and that the prices for the goods of the kind we are talking about here, which I referred to recently, shows that the present-day prices of those classes of materials are far higher than they were in 1943.

And finally, I say, of course, that it is not today's value in the sense of 1946 that you are to fix, but the value at the date of this statute when the rules were changed, when the new set-up was changed, and that is early in 1944.

Now, then, there is the question about this divided rate base, and I must say I have some difficulty in following it, and I do not mean to say that because I have difficulty in following it that there might not be anything in it. However, I think I should deal with it.

Now, Counsel for both the City and the Canadian Western, as I understand it, advanced and pressed the proposition that your Board, having arrived at the value of Madison's utility property, should adopt or include only a percentage of that value as Madison's rate base. Now, that is the proposition.

Now, Mr. Steer, in Volume 88, page 7178, said there, and took it arbitrarily, arbitrarily assumed, and I am using his words now, an equal division of the common costs of

Madison and Royalite. Having assumed that, he then asked your Board to allow Madison as rate base, 50% of the cost of the old and the new gathering lines, 25% of the unit service depreciated, and then he conceded that 100% of the scrubber costs, depreciated, 100% of the compression of the dry gas costs, but only 50% of the wet gas compressor, and he suggests that those percentages should constitute the Madison rate base.

(Go to page 7411).

Then apparently he has some concern that the Royalite absorption plant, which according to his witness, his engineering witness, is not necessary for the dry gas business may see fit to discontinue the use of the utility service and he therefore says in effect that the undivided half of it, the utility plant should be regarded as Royalite and should not be in this rate base at all. Or substantially that is what he says. And that if the Royalite does go out of the absorption plant business it would suffer its own capital loss. That is obviously the reason behind this suggestion of 50% rate base. Now I will assume that if the Royalite absorbs or takes the capital loss he would concede in common fairness then that the Royalite could deal with its half interest as it saw fit. In other words as I understand it, the proposition is that this undivided half interest in this rate base is not devoted to public service at all. It is not in the rate base. I suggest that in common fairness that if that takes place and if Royalite goes out of business, or whether it does not, it would be entitled to a partition of its property under certain circumstances and I merely raise that, sir, to show the proposition is not practical. That under circumstances such as this, the Madison might end up where it has only half a gathering system and that that half would not be able to do the job.

Now both Mr. Fenerty and Mr. Steer as I understand it have predicated their split rate base or the allocation of these charges on a 50-50 basis because they arbitrarily - and I would like to include Mr. Blanchard in this company because he has taken the same position this morning - they arbitrarily assume in the first instance and

it is a necessary hypothesis of their submission as I understand it, that Royalite's absorption plant enjoys benefits to that extent. And then Mr. Steer, and I am referring now to page 7160, further says that whether or not Royalite itself is benefitted in its plant operations and whether or not they become profitable by reason of these charges or otherwise, that your Board, sir, should assume, and I am suggesting they are asking you to base your assumption wholly on conjecture, that you should assume or conject that the Royalite absorption plant plus the Madison Gas Utilities system and plus the Imperial Oil Refinery operation are virtually one and that they are acting together and that their profit or no profit in any one of them is of no particular moment. Then he says he has precedent for that or authority for that. Or he has company for it because I have taken the position that the profits or losses of the parties served is of no moment to the utility. Of course I say, sir, in regulating and fixing utility charges the profit of the customer is of no moment or consequence because the utility rates should be fixed, allocated and scheduled on the impact of the service which the utility renders and on the utility's costs but not on the profits or losses of any of the customers. But I do suggest that in all fairness that if the profit is the basis of allocation, then every party served should have his rates fixed on the same basis and that in any case I submit that this board should have evidence before it as to profits and losses and merits and demerits and interconnections between all the parties that are going to be served and benefitted by this system.

MR. BLANCHARD: May I say that so far as I am concerned,

I am not suggesting this allocatinn of costs on the basis of benefit at all but on the basis of use. I would like to make that clear.

MR. FENERTY: Used and useful.

MR. CHAMBERS: Now, sir, as I understand it Mr. Steer relies on that Exhibit 177 as showing that the absorption plant has great benefits because it would cost so much to lay down Texas absorption gasoline here or Montana gasoline and that we have to assume, or your Board should assume that this gasoline that comes through or that it extracts in its absorption plant is worth that and it is paying so much less and therefore has great benefits. I submit, sir, that there is no evidence that the refineries necessarily require this kind of product and I think there is evidence, my recollection is that the refineries adjust their operations or their mechanism to the type of product that is available in the area. I do not think that Mr. Steer suggests for a moment that if there was no absorption gasoline in Turner Valley that these companies would bring in absorption gasoline from those places at those prices, I think Mr. Donellan's evidence is to the contrary.

Now then, of course, I also suggest that if the Board had the power - and I submit of course that they have not - but if it did have the power and should decide to fix rates of the absorption plant on the basis of benefits or joint benefits to the refinery, it should then in the interests of justice and reason proceed on the assumption and make provision for the making good of losses, because if you are going to have customers go off the line on the basis of their benefits or losses, the utilities will have no assurance that

they are going to receive the funds. So I submit, sir, the profit motive or the extent of the benefits becomes the test then you must take it both ways and that, in itself shows the absurdity of the situation.

Now one of the reasons that is advanced as I understand it by Mr. Fenerty for this 50-50 split rate base or this 50-50 costs allocation is that in his view the capacity of the utility gas gathering system has been and is now, as I take it, controlled and its demand costs substantially increased by the absorption plant, rather than by the fuel gas market. That is my understanding of the proposition he put up yesterday. My answer to that, sir, is simply this that the uncontradicted engineering evidence is to the direct contrary and rather is to the effect that the size and the capacity of the Madison's gas gathering system and its compression system are dictated by the fuel gas market demand. Furthermore I say that the engineering evidence, and there is no contradiction of it as I know of, is also to the effect that the wet gas content does not increase the gathering cost. Now that is the evidence of Mr. R. E. Davis, who was called on behalf of the Gas Company and Mr. Stevens-Guille says the same thing.

Now just a moment on book depreciation. My friend Mr. Fenerty argues, or rather he urges on you, and I rather gathered Mr. Steer does too, that book depreciation should be used in arriving at a present-day value and notwithstanding that every witness called dealt with the matter, including the government witness, these witnesses not only said they disagreed but they gave their reasons for it. As I understand it, Mr. Fenerty is now asking your Board that

notwithstanding that evidence and notwithstanding the fact that the City's witness or the City's advisor did not go into the box and submit to the test of cross-examination, he is asking your Board to take book depreciation. I put it merely on this ground that on the evidence, the entire weight of evidence is to the direct contrary.

Then I also refer to this, and I think it is of interest in the light of the discussion we had yesterday. . . . . I refer to the fact that the Federal Power Commission and the Hope Case in 1944, which was strongly relied on by my friend, Mr. Fenerty, in applying or computing these actual legitimate costs, did not deduct the Hope Company's book depreciation but that the amount they did deduct was less than the book depreciation to the extent of 25 million dollars. That, sir, is borne out by the report, 51 Public Utilities Reports, page 197.

The Supreme Court, United States judges have this to say in the judgment: It says:

> "It (the Commission) found that Hope during the years when its business was not under regulation did not observe 'sound depreciation and depletion practices' but 'accumulated an excessive reserve' of about $46,000,000.00. One member of the Commission thought that the entire amount of the reserve should be deducted from 'actual legitimate cost' in determining the rate base. The majority of the Commission concluded, however, that where as here, a business is brought under regulation for the first time and where incorrect depreciation and depletion practices have prevailed, the deduction

"of the reserve requirement (actual existing depreciation and depletion) rather than the excessive reserve should be made so as to lay 'a sound basis for future regulation and control of rates.'"

(Go to page 7417)

And then there is the footnote:-

" The book reserve for interstate plant amounted at the end of 1938 to about $18,000,000.00 more than the amount determined by the Commission as the proper reserve requirement. The Commission also noted that twice in the past the company has transferred amounts aggregating $7,500,000.00 from the depreciation and depletion reserve to surplus. When these latter adjustments are taken into account, the excess becomes $25,500,000.00'

and then it goes on:-

"'which has been exacted from the ratepayers over and above the amount required to cover the consumption of property in the service rendered and thus to keep the investment unimpaired."

And I say notwithstanding the implication that it was improperly extracted, when they came to fixing the rate base on the actual legitimate costs, they did not charge that up at all.

MR. FENERTY: So that my friend can deal with all at one time, I had that quotation in mind and I think I did say that that was a situation where improper depreciation practices had prevailed, and I think I called my friend's attention to the fact that there was no evidence here that the book depreciation taken was proper or improper.

MR. STEER: And that is exactly my position, I say the evidence discloses the probability that the company took improper depreciation in arriving at that.

MR. FENERTY : I had the same paragraph marked, that my friend read.

MR. CHAMBERS: Well, Sir, I say in any case that that

is an authority for that the company is not necessarily bound by its books, good, bad, or indifferent.

MR. STEER: I did not suggest that.

MR. CHAMBERS: But my friend, Mr. Fenerty, did yesterday.

MR. FENERTY: No, I am saying there is no evidence that it is proper or improper.

MR. CHAMBERS: But what I am referring to is the discussion which you had with the Chairman yesterday, and I say that during that discussion, either rightly or wrongly, I got the impression that the company must stand or fall on its books.

MR. FENERTY: I do not know about that.

MR. CHAMBERS: Now I want to touch on this question of "depreciation" in relation to the position taken by my friend, Mr. McDonald, on the throughput basis and as applying to the others also.

Now while my friend, Mr. McDonald, in his argument on behalf of the producers' committee took the position that reproduction costs new was not unreasonable or not improper, less depreciation, of course, he disagreed and the others did too, as well, as to the method or basis of arriving at the amount of that depreciation which is to be deducted.

Now I suggest, Sir, and Mr. McDonald can correct me if I am wrong, that he had no particular criticism of the fairness or the thoroughness or the technical knowledge of Mr. Hill as an engineer in making his inspection of the property, and assessing it, and giving us his true report on that phase of the situation. I rather gathered that Mr. McDonald

is opposed, and the others too are opposed, to the inspection or the observation method itself, of assessment, for determining the amount of existing depreciation, and that instead, Mr. McDonald recommends the reproduction cost new should be depreciated in the ratio that the past throughput bears to the total sum of the past throughput plus the estimate of the remaining reserves, and I rather gathered that if your Board should decide that reproduction costsnew was the proper basis, that all parties would say at least that depreciation on the throughput basis recommended by Mr. Hamilton should be used, and I might illustrate the point I desire to make by dealing with what Mr. McDonald said, because I think this sums the matter up:

At page 6982 he sums up the basis of his criticism or his objection by quoting extracts from Barnes "Economics of Public Utility Regulations" as illustrating why depreciation assessed on the observation method is inherently unsound, and that some other method should be used.

I am not going to quote all of it, but he says at page 6982:

> "Many and serious weaknesses beset the inspection method of measuring accrued depreciation, even in its more highly developed forms.'

and I gather from the context the "highly developed forms" means inspection, having in mind obsolescence and so on by the engineer giving consideration to other matters than the physical condition of the plant, and then he continued:

"In theory, depreciation proceeds from all those conditions which tend to limit the useful life of productive property. The inspection method, however, tends to narrow the search for depreciation to those aspects of the property which are susceptible of physical identification and measurements'.

and then:

(Go to page 7421)

"In procedure, the inspection method assumes that it is possible to forecast the remaining useful life of equipment and other property currently in use. As a matter of fact, it is quite impossible to forecast the useful life of most property without resort to the experience tables which are basic to the service-life method."

And then he goes on:

"To ask the engineer to forecast the remaining life of a generator, a pole line or a car, is like asking a doctor to predict the life of an individual; in either instance, if the condition of the property or the individual is critical enough, a forecast of an early end may be possible."

Now I submit, sir, to apply the accrued depreciation on the basis of the throughput, past and future, is a far more uncertain proposition because in the case of the engineer appraising a property he knows the property, he knows the plant and equipment, he knows whether the plant and equipment is in existence, and the plant and equipment that will do a better job, but the minute you appraise the existing value of a property to a considerable extent by basing it on how much gas is to be produced from a zone a mile beneath the surface of the ground over the next twenty-five years, I submit that that is in the same class, - if you cannot expect a doctor to predict how long a patient is going to live after seeing him, certainly you could not very well expect him to predict how long a patient whom he has never seen and whom he never will see, is going to live, and I say furthermore that it is not only unpredictable or unknowable so far as what is in the ground is concerned but this practice of production

depends to a large extent on the practice of other parties and upon innumerable other conditions over which this utility company or the owner of this property or the original vendor of the utility has no control whatsoever. In other words I submit that an estimate of accrued depreciation on the basis of the reserves in this field has all and far more of the weaknesses than any inspection method has and I submit, sir, that the proper method or the gauge of depreciation to be deducted is that which gives a lessening value to this plant because it is not a new and up-to-date plant, and Mr. Hamilton admitted that the throughput ignores altogether maintenance.

In the result I point out and I think my friend Mr. Blanchard dealt with it, that in any event on the throughput method your figures would be revised in the light of these estimates and in that connection I would like to make this clear, sir, that I gathered from Mr. Hamilton that while in his Exhibit 194 he has predicated his accrued depreciation on the known reserves, that he has not done it carefully, or in other words he told me, and I think my learned friend Mr. Blanchard will agree, that he has done it hurriedly and if that method is adopted there is to be a more definite check.

MR. BLANCHARD: Oh quite.

MR. CHAMBERS: And I would say this, sir, that I think that the parties and the owners of the properties involved, if that method is used, should be given an opportunity to be consulted so as to say "Well now if this is the figure', and I am sincere in this, sir, because there is some doubt in our minds as to how much the past should be taken into consideration and we should, I suggest, be appraised as to how it is suggested that it be divided. I think Mr. Hamilton's working papers have

never been studied, even on the old basis and I gathered that Mr. Hamilton had that in mind, that this other computation would be made.

MR. BLANCHARD: Yes, that is so.

MR. CHAMBERS: Now I would point out this, sir, that Exhibit 181, Schedule 1, shows the depreciable plant, on Hill's basis, adjusted as I outlined it, shows a depreciation of 21.6% and I am mentioning that to compare with the other figure which you suggested might be of interest, and for the purposes of the record in order to get that percentage, it is arrived at in this way:

There was the reproduction costs new of $3,002,325.97.

A depreciated figure comparable with $2,442,207.53;

And then we take off for working capital, going value and Girbotol royalty, $409,725.84, off each of those items.

And you get $2,592,600.13 new.

Depreciated to $2,033,481.69,

Or a total depreciation of $560,118.44,

Or the 21.6%.

Now in passing I would say this, that admittedly Exhibit 181 does not contemplate even for the future that any going value included in the rate base should be depreciated. Now I admit that is the basis of our request, on the basis that we have set it up it would be a rate of return carried over the period, and that we would never get anything back on the two hundred thousand, on the basis that I suggested.

Mr. Blanchard mentioned while he does not agree with going value, if it is included as worked out, that it should be depreciated the same as anything else and I do suggest on the method that we have mentioned that the amount payable over the period, may be less. I think it would be less. That is as far as I can go at the moment.

(Go to Page 7425)

In other words according to the computation of $83,981.00 for the Seaboard obsolescence was 21.6 on the depreciated asset . It is interesting to note that the approved depreciation on the straightline basis using Mr. Hamilton's WH-9 of Exhibit 124 where he shows his estimate of historical cost by years and acquisition works out at 21.05% computed on the following basis and just for the purpose of the record I show how I got that;

(a) Weighted average of the number of expired years, January 1st, 1944 of all the installations was 7.995 or say eight years, that is the -weighted average.

Secondly, that 7.995 years computation is arrived at by multiplying the 1943 installations by half a year, 1942 installations by a year and a half, and so on down the line, and dividing the sum of these answers by the total value of the installations.

That is how we arrive at that figure.

Then, thirdly, on the basis of all the assets being used and useful for thirty years. That is to the end of 1973 --and on that basis I say the weighted average percentage for depreciation is 21.05%.

Now on the other hand by taking the scrubbed gas throughput past and future as a means of estimating accrued depreciation and using the weighted average of installations as being eight years as of January 1st, 1944, all installations could be considered as having been made in 1936 and according to Mr. Hamilton's Exhibit 124, WH 12, the percentage depreciation accrued to the end of 1943 for the year 1936 was 18.6% on the basis of dry gas scrubbed, but that is by using the 336.7 billion cubic feet reserve at the end of

1943. And I understand that if we use the latest scrubbed gas reserve of 358.3 billion cubic feet the accrued depreciation would be around 17.6% on that basis.

Now I am mentioning this question of depreciation because I think it is well to have on the record, sir, the various computations to assist you.

THE CHAIRMAN: Is it not a little more than rebuttal ?

MR. CHAMBERS: Well this undoubtedly is sir, and it arose out of what you said during the course of my argument. You remember I mentioned -

THE CHAIRMAN: The comparison of straight line depreciation and the other.

MR. CHAMBERS: Yes, and merely for the sake of putting it in the record for convenience according to what I have said. I think Hill's percentage which is 21.6 straight line was 21.05. The accrued on the scrubbed gas unadjusted was 18.6. The average scrubbed gas adjusted is 17.6 and the average accrued estimated by Mr. Hamilton on those various bases, as I understand it, is 25.7.

Now I understand and gather that my friend Mr. Steer and I am referring to Page 7181 submitted in effect that Royalite should now be dealt with and held accountable as though it should have, when it started to develop the Turner Valley field, estimated the amount of capital which it would require over the whole life of the field and as though they set out in the first instance to apply a rate of depreciation on the entire amount of that capital. Now that was my appreciation of one of his submissions and now I say that proposition is not logical in developing new fields in the first oil field in this country under circumstances that no person could foresee.

Now to assess value or charges to a Company on the basis that it should have done that years ago I submit is not fairness in any sense of the term.

Now about the cost of repressuring. My friend, Mr. Fenerty said yesterday, sir that the cost of repressuring should not be included because there is no guarantee that the consumers will get it. Now I will refer merely to Mr. Ralph Davis who held a different view and I have already indicated that the guarantee will be given that it will be turned back to Madison within a reasonable time, but that is a matter for the Board to work out and I suggest the Board can make conditions under which the gas is to be taken. Dr. Katz stated that if the speculative element was taken out and that the prices would be frozen and I submit that is an added remuneration or boon to the market, but I suggest, sir, the only alternative is this, would be for the Board to order somebody if it has the power, and we will assume it has for the moment, to spend some money on it. I submit sir there is no power in the Board and I submit you should not and would not even if there was power under the Act, to order a party to spend money on gas in storage either in the gathering or paying those charges unless there is evidence to indicate a reasonable assurance that the party spending that money will not only get his money back but also get a return on it plus a return on some small amount of value that that gas has today.

My learned friend Mr. Blanchard submits that there is some intrinsic value of the gas at the bottom of the ground.

I submit, sir, it is not on the evidence before you an economic proposition to pay a rate of return

throughout the years on money spent on gathering this gas and I say if in the end the consumer has to pay all these charges he is worse off and by paying it now he avoids paying the interest charges and I say there is a precedent for that, the Bow Island field, as my learned friend says, or rather Mr. Davies as I understood him to say, that in the Bow Island the Gas Company is capitalizing and getting a return on it.

THE CHAIRMAN: They capitalized the purchase. I do not understand the capitalized repressuring cost.

MR. CHAMBERS: I do not know, but I rather gathered from what Mr. Davies said from his seat here yesterday that there was something being capitalized.

THE CHAIRMAN: I can understand they capitalized the value of the gas because it is like a commodity on your shelf.

MR. McDONALD: Mr. Brownie's evidence was that they were capitalizing the gas, the expense of putting it in and everything involved in it.

MR. STEER: He certainly did not give evidence they were capitalizing the cost of gas. They were capitalizing the cost of handling it.

MR. CHAMBERS: Then the other objection that my learned friend discussed was that his clients were fearful that this gas would be used for a Fischer-Tropsch process and that the City of Calgary consumer would be paying the cost of that in the rates and they would never get the benefit of it. All I can say that is one of the reasons for your Board to control the use of gas and then the Fischer-Tropsch or any other industrial process could not be set up to take gas from the Calgary market without your consent.

THE CHAIRMAN: Without compensation.

MR. CHAMBERS: Yes.

THE CHAIRMAN: Then I am going to adjourn now.

(At which time the Hearing was adjourned to be resumed at 10 A.M. June 21st, 1946)

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